

STATE OF CONNECTICUT

**AUDITORS' REPORT
CONNECTICUT DEVELOPMENT AUTHORITY
FOR THE FISCAL YEARS ENDED
JUNE 30, 1997, 1998, and 1999**

AUDITORS OF PUBLIC ACCOUNTS
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January 22, 2001

**AUDITORS' REPORT
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FOR THE FISCAL YEARS ENDED JUNE 30, 1997, 1998, and 1999**

We have made an examination of the books, records and accounts of the Connecticut Development Authority (CDA), as provided in Section 2-90, as amended, and Section 32-11a of the General Statutes, for the fiscal years ended June 30, 1997, 1998 and 1999.

SCOPE OF AUDIT:

The CDA is a quasi-public agency as provided for by Chapter 12 of the General Statutes. In addition to receiving annual financial audits by independent public accounting firms, the Authority received compliance audits, as required by Section 1-122 of the General Statutes. After having reviewed the reports and work of the outside firm and having satisfied ourselves as to the firm's independence, professional reputation, and qualifications, we have relied on those financial and compliance audits, in addition to internal control documentation. Comments in the independent auditor's reports are presented under the heading "Independent Audits" in this report. Financial statements of CDA are included in its annual reports for the fiscal years ended June 30, 1997, 1998 and 1999.

In accordance with Section 7 of Public Act 98-253, CDA has the authority to create subsidiaries to carry out the remediation, development, and financing of contaminated property within the State. As a result, CDA established the Connecticut Redevelopment Authority, Inc. (CRA). CRA was incorporated as a non-stock corporation on May 17, 1999, as a subsidiary of the Connecticut Development Authority. We will report on the activities of the CRA and other subsidiaries in the course of the audit of CDA.

We have limited our examination to such procedures as reviewing selected internal controls, adherence to various compliance requirements, and resolution of prior audit recommendations. This report on our examination consists of the Comments and Recommendations which follow.

COMMENTS

Foreword:

The Connecticut Development Authority, hereinafter referred to as CDA or the Authority, operates primarily under the provisions of Title 32, Chapter 579, Sections 32-11a through 32-23xx of the General Statutes. CDA is a body politic and corporate, constituting a political instrumentality and political subdivision of the State. The Authority's mission is to maintain and create jobs within the State by stimulating industrial and commercial development, primarily through financial assistance to businesses. In addition, the Authority has been responsible for operations at the Hartford Civic Center since September 1993.

Board of Directors and Administrative Officials:

Members of the CDA Board of Directors as of June 30, 1999, were as follows:

Ex officio Members:

- Denise L. Nappier - State Treasurer
- Marc S. Ryan - Secretary, Office of Policy and Management
- James F. Abromaitis - Commissioner, Dept. of Economic and Community Development

Appointed Members:

- Arthur H. Diedrick, Chairman
- Anthony J. Campanelli
- L. Scott Frantz
- Richard W. Glover
- Dennis Hrabchak
- Thomas F. Mullaney, Jr.
- Richard T. Mulready
- Anthony J. Nania

The chief executive officer (Executive Director) of the Authority is appointed by the Board. Antonio Roberto was appointed as the Executive Director on September 17, 1997, and served through the audited period.

Recent State Legislation:

During the audited period the General Assembly passed several laws which affected CDA. The major ones are summarized below:

- Public Act 98-253 permits CDA to create subsidiaries for the purpose of carrying out activities related to properties within the State that are environmentally contaminated. Such subsidiaries are deemed to be quasi-public agencies.
- Public Act 99-30 changed CDA's reporting requirements from semiannual to annual, establishing a November 1 deadline for submission.

Independent Audits:

As noted previously, CDA has been subject to annual audits by independent public accountants (IPAs) covering its financial statements and the compliance matters described in Section 1-122 of the General Statutes. For each of the fiscal years under review, the IPAs issued management letters presenting recommendations related to the internal control structure of CDA. Discussed below are summaries of the management letter findings and implemented resolutions resulting from the IPA's audits for the fiscal years ended June 30, 1997, 1998 and 1999.

In conjunction with the examination of the 1996-1997 financial records, a management letter on the internal control structure was issued on September 12, 1997. The letter contained three recommendations. These are summarized below:

- CDA should obtain assurances from vendors that CDA's computer systems are year 2000 compliant. CDA has since obtained the necessary assurances.
- Certain individuals were receiving salaries below the lower end of their established salary ranges. CDA has since corrected this situation.
- Information supporting the calculation of fair market value of equity investments was not fully documented. CDA has since corrected this situation.

In conjunction with the examination of the 1997-1998 financial records, a management letter on internal controls was issued on August 27, 1998. The letter contained six recommendations. These are summarized below:

- Certain equity investments classified as "available for sale" were not carried on the books at fair market value. The Agency defended its conservative approach.
- Access to the loan system by employees had not been updated to reflect changes in job function. CDA has since corrected this situation.
- The combination of the safe in which stock certificates are held was not changed after an employee with access was deemed to no longer need access. CDA has since corrected this situation.

- CDA needs to develop and test a comprehensive business-driven continuity program. CDA has not yet implemented this recommendation.
- CDA should implement controls requiring users to change their network and application passwords every 90 days. CDA has implemented corrective action.
- CDA should distribute security policies and procedures regarding the use of the Internet and e-mail to users. CDA has since corrected this situation.

In conjunction with the examination of the 1998-1999 financial records, a management letter on internal controls was issued on September 3, 1999. This report contained three recommendations in a letter dated September 15, 1999. These are summarized below:

- Audits should be performed to give CDA some assurance that the entity managing the Civic Center follows generally accepted accounting principles when reporting performance results. However, CDA is relying upon the contractor's internal audit reports and not independent audits. As a result of our review we have recommended that the CDA require annual audits of the contractor's operations in the future (See Recommendation 6.)
- The Authority does not have a written comprehensive Disaster Recovery Plan. The cost benefits of a "cold site" are being reviewed for hardware protection, and software files are now regularly backed up and kept off site.
- The division of duties and accounting procedures within the accounting unit are not formally documented. CDA issued a comprehensive Finance Department Manual in February 2000 that provided this information.

Connecticut Redevelopment Authority:

As mentioned previously, the Connecticut Redevelopment Authority (CRA) is a quasi-public agency created in accordance with Public Act 98-253. This entity was not created until May 1999 and did not have any financial resources available to it until that time, at which point CDA authorized \$1.5 million to CRA. No expenditures occurred during the period ended June 30, 1999. Subsequent audits will provide more detail of CRA's financial activities.

RÉSUMÉ OF OPERATIONS:

The Department of Economic and Community Development (DECD) provides CDA with advance funding to operate certain programs. This advance funding is financed with the proceeds of State bonds. Additional financing is obtained through the collection of various fees. CDA is also authorized to issue general obligation bonds for certain programs. Pursuant to Subsection (a) of Section 32-23j of the General Statutes, those bonds "...shall not be deemed to constitute a debt or liability of the state..." These bonds, except for issues totaling \$30,560,000

associated with the purchase of the assets of the Hartford Whalers, are secured by special capital reserve funds. CDA is required to maintain, in these funds, a minimum balance at least equal to the greatest principal and interest payments becoming due in the succeeding calendar year. If CDA is unable to maintain a sufficient balance in the special capital reserve fund, the State's General Fund could be required to restore the special capital reserve fund to its minimum balance if the specific bond indenture calls for such State reimbursement. (No such State payment was required during the audited period.) As of June 30, 1999, CDA's bonds payable amounted to \$115,500,197.

In addition, CDA is authorized under its Self-Sustaining Bond program to accommodate the financing for specific industrial and certain recreational and utility projects through the issuance of special obligation industrial revenue bonds. These bonds are payable solely from participating companies and are not otherwise a debt or liability of CDA or the State. Accordingly, the balances and activity of the Self-Sustaining Bond Program are not included in CDA's financial statements. Total bonds outstanding as of June 30, 1999, was \$1,080,700,222.

CDA maintains the following funds to account for its operations and various programs:

General Operating Fund:

CDA's operating expenses are recorded in its General Operating Fund and allocated net of Operating Fund revenue to its various programs. In addition, the Operating Fund is used to account for CDA's operation of the Hartford Civic Center.

Based on the Authority's financial statements, receipts of the Operating Fund totaled \$11,045,948, \$15,925,747 and \$17,181,062 for the 1996-1997, 1997-1998 and 1998-1999 fiscal years, respectively. Operating expenses for the same periods amounted to \$13,434,956, \$19,845,109 and \$20,085,967. The Operating Fund's respective net income/(loss), exclusive of unrealized holding gains/losses, amounted to \$(2,389,008), \$(3,919,362) and \$(2,904,905). The Hartford Civic Center's operations account for 100 percent of the losses.

Exclusive of the costs of running the Civic Center and interest payments, payroll and related fringe benefits were the single largest line-item expenditure category. Payroll and related charges for the three years under review were \$3,342,625, \$3,231,134 and \$3,287,344 respectively.

Umbrella Program Fund:

Under the Umbrella Program, CDA is authorized to issue bonds to provide financial assistance for the acquisition of land, buildings, new machinery, equipment and pollution control facilities. Loans up to \$800,000, with up to a 20-year term, can be made for each approved project. Of this amount, up to \$500,000 can be used for machinery and equipment (term may not exceed ten years) and up to \$800,000 can be used for pollution control facilities (term may not exceed ten years.) Loans in this program are insured under to the Insurance Program (discussed later). During fiscal years 1996-1997, 1997-1998 and 1998-1999, \$33,919, \$874,260 and \$0 of defaulted loans were absorbed by the Insurance Program Fund.

Insurance Program Fund:

Authorized by Section 32-14 of the General Statutes, the Authority may insure loans made by other lending institutions to companies for the acquisition of industrial land, buildings, machinery, and equipment located within the State. In addition, all of the Authority's Umbrella Program loans are insured under this program.

As of June 30, 1997, 1998 and 1999, loans totaling \$59,828,137, \$49,939,101 and \$43,278,621 respectively, were insured as follows:

	<u>1999</u>	<u>1998</u>	<u>1997</u>
Loans by other lending institutions	\$ 8,830,196	\$ 8,869,326	\$ 9,585,757
Umbrella Program loans	34,448,425	41,069,775	50,242,380

Growth Fund:

In accordance with Section 32-23v of the General Statutes, CDA is authorized to issue individual Growth Fund loans up to a maximum of \$4,000,000 with a maximum loan term of 20 years. The program provides financial assistance for any purpose the Authority determines will materially contribute to the economic base of the State by creating or retaining jobs, promoting exports, encouraging innovation or supporting existing activities. Financing may be used to purchase real property, machinery and equipment, or for working capital.

The Authority has established a maximum 90 percent loan-to-value ratio for real property loans and 80 percent loan-to-value ratio for machinery and equipment loans. Working capital loans are limited to a term of up to seven years.

A summary of the Growth Fund's lending activity for the last three years is as follows:

Fiscal Year Ended	Number of Entities	Assistance
<u>June 30,</u>	<u>Receiving Assistance</u>	<u>Provided</u>
1997	23	\$10,626,445
1998	23	11,037,909
1999	34	10,364,223

Connecticut Works Fund:

The Connecticut Works Fund, also known as "Fund A", is established in accordance with Section 32-23ii of the General Statutes. The Fund is used for either direct loans or loan guarantees. Eligible projects include most manufacturing-related projects and any project that supports the economic base of the State through jobs, defense diversification, exporting and the development of innovative products or services.

The State has authorized the issuance of up to \$128,000,000 in State bonds allocated to Fund A. Of this amount, \$82,485,000 has been distributed to Fund A. In the event direct loans

are uncollectible, CDA can use any remaining bond funds to reimburse itself for such losses, up to \$15,000,000 per loan, subject to the total allocation.

A summary of Fund A's lending activity for the last three years is as follows:

Fiscal Year Ended <u>June 30,</u>	Number of Entities <u>Receiving Assistance</u>	Guarantee <u>Provided</u>
	<u>Loan Guarantees:</u>	
1997	1	\$3,800,000
1998	0	-0-
1999	0	-0-
	<u>Direct Loans:</u>	
1997	9	\$11,371,170
1998	10	21,597,137
1999	12	13,974,369

Connecticut Works Guarantee Fund:

The Connecticut Works Guarantee Fund, also known as "Fund B", is established in accordance with Section 32-261 of the General Statutes. The purpose of Fund B is to provide commitments to guarantee loans made by participating financial institutions. Projects financed by the program are intended to encourage growth and the retention of businesses unable to obtain suitable financing and to stimulate an increase in jobs and tax revenue throughout the State. Eligibility is determined by the due diligence principles set forth in the Connecticut Works Fund.

The State has authorized up to \$39,000,000 in State bonds allocated to Fund B. Of this amount, \$10,000,000 has been distributed. In the event direct loans are uncollectible, CDA can use any remaining bond funds to reimburse itself for such losses, up to \$10,000,000 per loan, subject to the total allocation.

A summary of the Fund B's activity for the last three years is as follows:

Fiscal year Ended <u>June 30,</u>	Number of Entities <u>Receiving Assistance</u>	Guarantees <u>Provided</u>
1997	10	\$14,280,357
1998	9	5,161,560
1999	9	3,734,225

Connecticut Capital Access Fund:

In accordance with Section 32-265 of the General Statutes, the Connecticut Capital Access Fund provides portfolio insurance to participating financial institutions to assist them in making loans that are somewhat riskier than conventional loans. These loans are of two types,

referred to as Urbank Program loans and Entrepreneurial Program loans. Project eligibility is usually determined by the financial institution making the loan, subject to requirements specified in participation agreements. Separate loan loss reserve accounts are established to cover losses on enrolled loans.

The State has authorized the issuance of up to \$5,000,000 in State bonds allocated to this Fund. Of this amount, \$2,000,000 has been distributed. In addition, any insurance losses associated with this Fund are reimbursable from those bonds up to the \$5,000,000 allocated.

A summary of the Fund's lending activity during the last three years is as follows:

Fiscal Year Ended <u>June 30,</u>	Number of Entities <u>Receiving Assistance</u>	Amount of Assistance <u>Provided</u>
1997	48	\$ 717,367
1998	66	1,206,635
1999	48	398,717

Business Environmental Clean-Up Revolving Loan Fund

Established in accordance with Section 32-23z of the General Statutes, this Fund provides direct loans to assist businesses in the containment or removal of property contamination. To be eligible, the business must have been established at least one year in the State, have sales of less than \$3,000,000 or less than 150 employees, and be unable to obtain conventional financing. Loan amounts cannot exceed \$200,000.

No loans were made from this fund during the audit period and there is no additional funding available for this program.

Environmental Assistance Revolving Loan Fund:

Established under Section 32-23qq of the General Statutes, CDA can use the Environmental Assistance Revolving Loan Fund to provide direct loans and guarantees to businesses to assist in financing pollution prevention activities or purchases and costs associated with the installation of stage II vapor recovery systems. To be eligible, an entity must have revenues of less than \$25,000,000, or fewer than 150 employees. There has been no loan or guarantee activity since August 1996.

Fiscal Year Ended <u>June 30,</u>	Number of Guarantees <u>Issued</u>	Total of <u>Guarantees</u>
1997	1	\$10,000
1998	0	0
1999	0	0

Job Training Fund:

This Fund was established to account for the Connecticut Job Training Finance Program authorized by Section 32-23uu of the General Statutes. Assistance under this program is provided to manufacturing or economic base businesses seeking to provide educational upgrades to their production workers. Performance grants of up to \$25,000 are available, covering up to 25 percent of the amount borrowed by each business.

Funding for this program is provided by the bond issue authorized under Sections 32-23ll and 32-235 of the Statutes.

Fiscal Year Ended <u>June 30,</u>	Number of Entities <u>Receiving Assistance</u>	Amount of Assistance <u>Provided</u>
1997	6	\$104,950
1998	34	610,387
1999	38	807,301

Summary of Revenues, Expenses and Net Income:

Based on CDA's audited financial statements, the following is a summary of the revenues, expenses and income of the consolidated operations for the fiscal years ended June 30, 1997, 1998 and 1999.

	<u>1997</u>	<u>1998</u>	<u>1999</u>
Revenues:			
Civic Center revenues	\$ 7,324,489	\$ 11,444,918	\$13,482,774
Premiums earned	1,722,598	1,467,926	841,166
Interest on loans	11,142,521	10,822,009	10,680,171
Investment income	5,082,715	5,168,359	4,592,507
Other	<u>2,000,773</u>	<u>2,643,256</u>	<u>3,164,397</u>
Total Revenues	<u>27,273,096</u>	<u>31,546,468</u>	<u>32,761,015</u>
Expenses:			
Civic Center expenses	9,713,497	15,364,280	16,387,679
Interest	7,102,342	6,739,976	6,419,869
Payroll and fringe benefits	3,342,625	3,231,134	3,287,344
Other	<u>1,847,409</u>	<u>2,148,189</u>	<u>2,310,009</u>
Total Expenses	<u>22,005,873</u>	<u>27,483,579</u>	<u>28,404,901</u>
Net Income:	<u>\$ 5,267,223</u>	<u>\$ 4,062,889</u>	<u>\$ 4,356,114</u>

Summary of Loan Write-Offs and Guarantee Claims Paid:

Based on data in CDA's internal financial reporting package the following is a summary of the loan amounts written off and guarantee payments made and the written-off loans recovered and written-off guarantees recovered for the fiscal years ended June 30, 1997, 1998 and 1999:

<u>Fiscal Year Ended June 30,</u>	<u>Direct Loans Written off</u>	<u>Guarantees Paid</u>	<u>Loans Recovered</u>	<u>Guarantees Recovered</u>
1997	\$ 967,830	\$1,027,425	\$ 974,562	\$ 956,393
1998	2,655,407	1,323,575	760,101	72,134
1999	2,182,024	1,717,623	445,232	20,206

CONDITION OF RECORDS

Our limited examination of the records of the Connecticut Development Authority revealed certain areas requiring attention. These areas are detailed in this section of the report.

Statutory Reporting Requirements:

Criteria: Section 32-1i of the General Statutes requires that the Commissioner of Economic and Community Development (DECD), in conjunction with the executive directors of CDA, Connecticut Innovations Incorporated, and the Legislative Program Review and Investigations Committee, develop improved objectives, measures of program success and standards for granting financial and non-financial assistance under programs administered by DECD and the Authority. Said Section requires that the Commissioner and said executive directors prepare annual reports analyzing the performance of programs in accordance with those objectives.

Section 32-3 of the General Statutes grants the Authority access to all available information collected by any State agency.

Section 32-11a, subsection (c), of the General Statutes details the specific contents of reports that the Authority is required to submit on an annual basis to DECD, the Auditors of Public Accounts, and various legislative committees.

Sections 32-475 through 32-480 of the General Statutes establish a high performance work environment program. Section 32-479 requires that CDA, in conjunction with the Commissioner of Economic and Community Development, the Labor Commissioner, and Connecticut Innovations, Inc., jointly develop goals and objectives and quantifiable outcome measures for the program by July 1, 1996. An annual report concerning such goals and objectives should be submitted to the cognizant joint standing committees of the General Assembly.

Condition: The performance measures and objectives required by Section 32-1i were never established by DECD. Hence, the required reporting could not be performed by CDA.

There has been a notable improvement in the completeness of the Authority's reporting under Section 32-11a of the Connecticut General Statutes. However, the Authority's annual report for the fiscal year ended June 30, 1999 did not include certain required data. The reporting requirements in Section 32-11a, subsection (c) of the General Statutes refer to data (wage and employment figures and gross revenues) that is typically collected by the Departments

of Labor and Revenue Services. The Authority had engaged a public accounting firm to collect most of the labor-related data that it needs for its reports. The firm used survey methods without reconciling the survey data to financial information submitted and certified to the Departments of Labor and Revenue Services. The Authority explained that it had to do this because it was difficult to get the information required from the Department of Labor in a timely manner.

In addition, there exists a question as to whether the revenues of specific companies can be reported without violating the confidentiality provisions of Section 32-11a, subsection (k). As a result, CDA reported the number of companies within certain ranges of revenue without identifying each company. While this method maintains confidentiality, it does not appear to conform to the requirement that such data be reported "for each recipient".

The Authority has not been preparing an annual report as required by Section 32-479 of the General Statutes.

- Cause:* A lack of administrative control contributed to these conditions.
- Effect:* The Authority's legislated reporting requirements were not fully complied with. The Authority is providing costly and incomplete data obtained by the use of survey techniques and not taking full advantage of the availability of complete information at no cost to the Authority from the State agencies. It appears that the Authority is being requested to report data that is protected under the provisions of Section 32-11a, subsection (k).
- Recommendation:* The Authority should implement procedures to comply with all of its legislated reporting requirements and expand efforts to obtain information from State agencies in order to verify statistics reported by borrowers. Where questions exist as to the confidentiality of required information, CDA should seek legislative clarification to ensure that the legislative intent is met. (See Recommendation 1).
- Agency Response:* "The CDA issued its comprehensive annual statutory report on September 30, 1999 in accordance with Section 32-11a of the General Statutes. The CDA currently obtains its data from using surveys, direct calling methods, and through the normal course of business as we deal with each transaction. In future reports the CDA will augment its past practices and review whether contacting the Department of Labor and the Department of Revenue Services to obtain the specific data will facilitate the fact gathering process. In addition, the CDA will try to obtain

legislative clarification where a question exists as to the confidentiality of the required information.

The CDA has various goals and objectives for each fiscal year. These goals and objectives are measured each year through various financial and statistical reports. Some of these reports include: Annual Audited Financial Statements, Compliance Report, Cluster Report, Jobs Retained and Created Report, The Minority Assistance Report and the Legislative Annual Report submitted each fall to the Legislature.

The CDA has established the procedures to obtain the required goals and objectives as required under Section 32-479 of the General Statutes. The CDA will comply with the reporting requirements under Section 32-479 of the General Statutes.”

Staffing of the Governor's Regional Offices:

Criteria: Budgetary constraints in the form of authorized appropriations and positions are intended to provide a level of control over agency spending. Section 32-3 of the General Statutes states that CDA shall assist, as appropriate, other State agencies in their duties upon request.

Condition: The Governor's Bridgeport and Norwich offices have three employees and one employee, respectively, charged to the payroll of the Authority. Monthly activity reports submitted by these employees indicate that much of their time is spent with social service agencies and Governor's Office initiatives that are not directly related to CDA activities. In addition, the entire lease payment for the Bridgeport office is paid by the Authority without any reimbursement being received from the Governor's Office.

Cause: The Authority believes that the efforts of these employees contribute to the overall community development in their respective regions and as such their costs are a legitimate charge against the Authority's budget.

Effect: The cost of operating the Governor's Office and CDA are erroneously stated. In addition, the failure of the Governor's Office to charge all expenses to the proper State General Fund budgetary account weakens legislative budgetary control.

Recommendation: The cost of CDA employees' time used to provide services to the Governor's Office should be properly allocated. (See Recommendation 2).

Agency Response: “CDA disagrees. The Governor’s Office assigned the persons in question to the Bridgeport and Norwich regional offices in order to advance CDA’s mandate of facilitating economic development in these hard-pressed areas. In our view, any activity that promotes directly or indirectly economic development in these regions “benefits” the CDA. We believe the State Auditors are taking too narrow a perspective of the CDA’s mission and what is needed to spur economic development in the State. Nevertheless, CDA will work with the Auditors to attempt to devise a system of accounting for the time and effort of these employees that is responsive to the Auditors’ concerns.”

Auditors’ Concluding

Comment: Previous audit responses from both CDA and the Governor’s Office have essentially been the same. However, the condition continues to prevail without evidence of any attempt to devise a system.

Severance Payments to Employees:

Criteria: In accordance with Section 1-121 of the General Statutes, the Authority has established written policies for most payroll/personnel matters.

Condition: Our prior audit noted that severance payments were made to separated employees without the existence of specific policy pertaining to the matter. While only one such payment was noted currently, there continues to be a lack of policy on such payments.

Cause: The Authority has not seen the need for a severance policy, preferring instead to have severance arrangements approved individually by the Board of Directors.

Effect: The lack of a formal policy for the payment of such benefits could lead to apparent inconsistencies, the appearance of favoritism or the appearance of discrimination.

Recommendation: The Authority should establish policies and guidelines relative to the payment of severance benefits. (See Recommendation 3).

Agency Response: “The CDA currently has all severance packages approved individually by the Board of Directors. The CDA will formalize this policy by establishing a written procedure as it relates to severance payments.”

Auditors’ Concluding

Comment: Formalizing the policy that severance packages will receive Board approval does not appear, by itself, to ensure consistent treatment.

Written procedures should include guidelines for eligibility and payment amounts.

Role of the Authority Chairman/President:

Criteria: Section 32-11a, subsection (c), of the General Statutes provides that the Governor shall appoint the Chairperson of the Board, with the consent of the General Assembly. The Chairperson is regarded as a voting member of the Board. Said Statute also provides that members of the Board shall receive no compensation.

Section 32-11a, subsection (f), of the General Statutes states that the board of directors of the Authority shall appoint an Executive Director who shall serve at the pleasure of the Board and not be a member of the Board.

Section 32-23e, subdivision (18), of the General Statutes permits the Authority to "employ such assistants, agents, or other employees as may be necessary or desirable for its purposes".

Condition: Changes that were made to the Authority's bylaws during the 1994-1995 fiscal year permit the Chairman, who is appointed by the Governor, also to serve the Board in the position of President, which is a paid position. The President is allowed a vote on board matters that do not affect his/her conditions of employment. Such an arrangement appears to violate the provisions of Section 32-11a, subsection (c).

Our prior audit pointed out that the Authority had essentially replaced the title of Executive Director with that of President. As noted previously, the Authority appointed an Executive Director (chief administrative officer) in September 1997. However, the President continues to receive compensation, functioning as the chief executive officer.

Cause: The Authority believes that such action is allowable under Section 32-23e, subdivision (18) of the General Statutes.

Effect: There is a possible conflict of interest inherent in having an appointed Chairman of a Board also serving as an employee of the authority over which the board has executive authority. In addition, the provisions of Section 32-11a, subsection (c) are not being adhered to.

Recommendation: The Authority should review the appropriateness of the appointment of the Chairman to the position of President under Section 32-23e, subdivision (18) of the General Statutes. (See Recommendation 4).

Agency Response: “The CDA has received an opinion from counsel that the appointment of the Chairman to the additional position of President is appropriate.”

Auditors’ Concluding

Comment: The opinion from CDA’s counsel is based on the assumption that Section 32-11a, subsection (c), means that a member cannot be compensated for services rendered as a Board member, rather than an employee. Said Section does not appear to differentiate between compensation as a Board member versus compensation as an employee. The Authority should seek an opinion on this matter from the Office of the Attorney General.

Lack of False Statement Provisions on Loan Documents:

Criteria: Section 53a-157b of the General Statutes makes it a Class A misdemeanor to intentionally make a false statement intended to mislead a public servant in the performance of his duties, pursuant to a form bearing notice, authorized by law, that false statements are punishable by law.

Section 36a-56 of the General Statutes provides for penalties of false statements for those entities covered under the banking laws of the State of Connecticut, including first or second mortgage lenders. The Authority does not appear to meet the definition of any of the types of institutions covered by the banking laws.

Condition: Authority documents did not contain false statement provisions. While nothing came to our attention to indicate that any borrowers had made a false statement, we noted that the Authority appears to lack the legal authorization to incorporate such provisions into any of its documents, despite the fact that similar entities falling under the jurisdiction of State banking laws have such ability.

Cause: The Authority maintains that a material misrepresentation would lead to a loan default, enabling CDA to call the loan and foreclose if necessary. Therefore, false penalty provisions are unnecessary.

Effect: Public funds may be at greater risk if appropriate penalties are not in place to discourage false statements.

Recommendation: Legislation should be sought that would give the Authority a legal basis to include false statement penalties on its documents, similar to banking institutions (See Recommendation 5).

Agency Response: “Legislation will be sought that would give the CDA a legal basis to include false statement penalties on its documents.”

Management of the Hartford Civic Center Operating Agreement:

Criteria: Section 8.03 of the Hartford Civic Center Operating Agreement between the Authority and Madison Square Garden CT, LLC (MSG) dated August 1, 1997, states in part "The Authority shall be entitled at any time and from time to time within three (3) years after the receipt or payment of any fees, commissions or other payments to inspect the sufficiency and/or accuracy of any statement furnished by MSG in support of MSG's calculation thereof and to conduct an audit or examination of MSG's books and records".

Section 8.05 paragraph (a) of said agreement states in part "Not more than seventy-five (75) days after the end of each fiscal year, MSG shall deliver to the Authority, certified by independent public accountants reasonably acceptable to the Authority...full and complete financial statements with respect to MSG's operation of the Managed Facilities and Concessions including all customary Income and Expense statements, reconciliations and comparisons to projections, together with a statement of Gross Revenues, Operating Expenses and Net Profits for such Fiscal Year...".

Condition: The Authority has never requested an audit or examination of MSG's books as provided for in the operating agreement.

Cause: The Authority stated that it was relying upon two processes: the annual audit of the Authority itself (which addresses Civic Center revenues and expenses), and an Independent Accountants' Report on the application of agreed upon procedures with respect to the internal control structure implemented by the management of the concession operations.

The annual Authority audit does consider Civic Center revenues and expenses. However such data contains significant items which affect CDA's accounts but not those of MSG. In addition the scope of audit work conducted in relation to MSG's operations would be much greater in a specific audit of MSG than the CDA audit.

The agreed-upon procedures referred to above were performed to assist the CDA in evaluating the adequacy of and adherence to the internal control policies and procedures established by management. The sufficiency of the procedures is the sole responsibility of the CDA. No representation was made regarding the sufficiency of the procedures.

Effect: The use of the CDA audit and the agreed-upon procedures engagement does not satisfy either the terms of the Agreement cited above or their apparent intent.

Recommendation: The Authority should ensure that audit and reporting provisions in the Civic Center agreements are fully complied with. (See Recommendation 6.)

Agency Response: “The CDA agrees and will receive an audit for the year ending June 30, 2000.

Bidding Procedures for Civic Center Improvements:

Criteria: Pursuant to Section 32-11a of the General Statutes, the CDA is required to establish procedures over the acquisition of goods and services.

General procurement practice requires that the acquisition of goods or services should, when practical, be made on a competitive sealed-bid basis to help assure that the best possible price is obtained. Invitations to bid should be widely disseminated in order to attract a wide and well-qualified pool of applicants.

Condition: The Authority does not publicly invite applications for bids on major Civic Center projects, relying instead upon their consultant engineer and facility consultant who invite applications from candidates known to them.

Cause: Because of the limited time available for construction work at the Civic Center, the Authority believes it is best served by limiting the time taken for the solicitation and bid review process. To this end the Authority finds it more efficient to invite bids directly from firms known to their consultants rather than openly soliciting bids.

Effect: There is decreased assurance that the bidding process is equitable and that the most competitive pricing is being obtained.

Recommendation: The Authority should establish written procedures over the bidding process for major Civic Center purchases. In doing so, consideration should be given to requiring publication of invitations to bid. (See Recommendation 7.)

Agency Response: “The CDA’s practice is to receive at least three bids for all capital expenditures that are material in price. The CDA also will accept bids from any firm that wishes to participate in the bidding

process. The CDA will codify these practices into written procedures.”

Activities of Board Members:

- Criteria:* The State has established a Code of Ethics for State Officials that outlines conditions that could present conflicts of interest. Section 32-11a, subsection (h), of the General Statutes permits a Board member with a financial interest in a borrower to serve on the Board without presenting a conflict of interest, provided certain disclosures are made and the member abstains from voting on behalf of issues that would specifically impact the member.
- Condition:* During the audited period, a former member of CDA’s Board evaluated the status of a company that was thought to be in financial difficulty. After investigating the company’s prospects, the Board member was found to be negotiating with CDA staff on behalf of the company that was now partially owned by the Board member. These activities preceded the member’s resignation from the Board. While the CDA Board never approved subsequent financing to the company, the appearance of a Board member before CDA staff presents the appearance of a conflict of interest.
- Effect:* Permitting activities that present the appearance of a conflict of interest, even if not technically in violation of ethics laws, reduces public confidence in the process. In addition, since CDA Board members approve operating budgets and thus indirectly approve staff salaries, CDA staff may feel pressure to recommend financing arrangements that would normally not be approved.
- Cause:* CDA does not have a policy outlining the conditions under which a Board member may negotiate in front of the Board for financial assistance.
- Recommendation:* CDA should establish policies addressing the extent to which Board members may represent businesses with which they are associated in front of the Authority. (See Recommendation 8).
- Agency Response:* “The CDA agrees and will establish policies addressing financing requests from companies that are associated with Board members.”

RECOMMENDATIONS

Our prior audit contained 10 recommendations, three of which have been adequately resolved. The seven remaining recommendations have been repeated or restated to reflect current conditions. One additional recommendation has been formulated as the result of our current review. The status of those recommendations is presented below:

Prior Audit Recommendations:

- The Authority should improve its procedures to enable it to comply with its various reporting requirements in a complete and timely fashion. In addition, the Authority should consult with the Departments of Labor and Revenue Services, along with the Attorney General's Office, regarding the potential confidentiality issues presented by exercising CDA's authority under Section 32-3 of the General Statutes. This recommendation is being repeated. (See Recommendation 1).
- The cost of CDA employees' time provided to the Governor's Office should be properly allocated. This recommendation is being repeated. (See Recommendation 2).
- The Authority should consider revising its purchasing policies and procedures to provide for competitive bidding and improved internal controls. This recommendation has been modified to reflect current conditions. (See Recommendation 7).
- The Authority should adopt a formal policy for the payment of severance benefits. This recommendation is being repeated. (See Recommendation 3).
- The Authority should review the assignment of the titles of President, Chairman and Executive Director and insure that the applicable statutes are adhered to. This recommendation is being repeated. (See Recommendation 4).
- Legislation should be sought that would give the Authority a legal basis to include false statement penalties on its documents, similar to banking institutions. This recommendation is being repeated. (See Recommendation 5).
- Controls over threshold projects should be improved to insure compliance with statutory provisions. This finding has been adequately resolved.
- The Authority should increase efforts to comply with the prior notice requirements of Section 1-121 of the General Statutes. This finding has been adequately resolved.
- Efforts to maintain evidence of borrowers' insurance coverage and financial performance data should be improved. This finding has been adequately addressed.
- The Authority should take steps to insure that Civic Center vendors have an adequate internal control system in place to provide assurance that revenues are properly

recorded. This recommendation has been restated to reflect current conditions. (See Recommendation 6).

Current Audit Recommendations:

- 1. The Authority should implement procedures to comply with all of its legislated reporting requirements and expand efforts to obtain information from State agencies in order to verify statistics reported by borrowers. Where questions exist as to the confidentiality of required information, CDA should seek legislative clarification to ensure that the legislative intent is met.**

Comments:

CDA was not meeting the reporting requirements of Sections 32-1i and 32-479 of the General Statutes. Reporting requirements of Section 32-11a, subsection (c), were generally being met, but specific borrower information was being reported in the aggregate to maintain confidentiality of the data.

- 2. The cost of CDA employees' time used to provide services to the Governor's Office should be properly allocated.**

Comments:

We continued to note that the Governor's Office receives the benefit of office space and personal services of regional offices without charge. CDA incurs ongoing charges for service that are only partly related to its operations.

- 3. The Authority should establish policies and guidelines relative to the payment of severance benefits.**

Comments:

While only one severance payment was made during the audited period, we noted the continuing lack of a policy relating to such separation payments.

- 4. The Authority should review the appropriateness of the appointment of the Chairman to the position of President under Section 32-23e, subdivision (18) of the General Statutes.**

Comments:

Section 32-11a, subsection (c), of the General Statutes provides that members of the CDA Board shall not receive compensation. Changes made to the Authority's bylaws permit the Chairman, who is appointed by the Governor, to also serve in the position of President, which is a paid position. While the Authority claims that

Section 32-23e, subdivision (18) authorizes such an appointment, it appears that the intent of that Section is to permit the hiring of general staff rather than a chief executive officer.

5. Legislation should be sought that would give the Authority a legal basis to include false statement penalties on its documents, similar to banking institutions.

Comments:

Authority documents did not contain false statement provisions. While nothing came to our attention to indicate that any borrowers had made a false statement, we noted that the Authority appears to lack the legal authorization to incorporate such provisions into any of its documents, despite the fact that similar entities falling under the jurisdiction of State banking laws have such ability.

6. The Authority should ensure that audit and reporting provisions in the Civic Center operating agreement are fully complied with.

Comments:

At no time has the Authority had an audit or examination of MSG's books as provided for under Sections 8.03 or 8.05 (a) of the Civic Center operating agreement.

7 The Authority should establish written procedures over the bidding process for major Civic Center purchases. In doing so, consideration should be given to requiring publication of invitations to bid.

Comments:

The Authority does not invite applications for bids on major Civic Center projects by newspaper advertising, relying instead upon their consultant engineer and facility consultant who invite applications from candidates known to them.

8. CDA should establish policies addressing the extent to which Board members may represent businesses with which they are associated in front of the Authority.

Comments:

Section 32-11a, subsection (h), of the General Statutes permits CDA Board members to serve even if they have a financial interest in a CDA borrower. The absence of guidelines increases the risk that Board members could be placed in situations that have at least the appearance of a conflict of interest.

CONCLUSION

In conclusion, we wish to express our appreciation for the cooperation and courtesies extended to our representatives by the personnel of the Connecticut Development Authority during the course of our examination.

Kenneth Post
Principal Auditor

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts

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