

# STATE OF CONNECTICUT



*AUDITORS' REPORT  
CONNECTICUT HEALTH AND EDUCATIONAL FACILITIES AUTHORITY  
FOR THE FISCAL YEARS ENDED JUNE 30, 2010 and 2011*

**AUDITORS OF PUBLIC ACCOUNTS**

JOHN C. GERAGOSIAN ❖ ROBERT M. WARD

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# STATE OF CONNECTICUT



## AUDITORS OF PUBLIC ACCOUNTS

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November 19, 2012

### **AUDITORS' REPORT CONNECTICUT HEALTH AND EDUCATIONAL FACILITIES AUTHORITY FOR THE FISCAL YEARS ENDED JUNE 30, 2010 and 2011**

We have examined the books, records and accounts of the Connecticut Health and Educational Facilities Authority (Authority) as provided in Section 2-90 and Section 1-122 of the General Statutes, for the fiscal years ended June 30, 2010 and 2011.

#### **SCOPE OF AUDIT:**

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

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

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

Our audit included a review of a representative sample of the Authority's activities during the fiscal year in the five areas identified above and a review of such other areas as we considered

necessary. The financial statement audit of the Authority, for the fiscal years indicated above, was conducted by the Authority's independent public accountants.

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

## COMMENTS

### FOREWORD:

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

The purpose of the Authority is to assist certain healthcare institutions, institutions of higher education, and qualified not-for-profit institutions in the financing and refinancing of projects undertaken in relation to programs of the institutions. The Authority is empowered to issue its own bonds, bond anticipation notes and any other obligations for any of its corporate purposes and to fund and refund the same. As of June 30, 2011, CHEFA had issued \$13,801,053,000 in bonds, of which \$7,570,456,000 is outstanding. The Authority issued general obligation bonds through June 1979, for which the Authority is ultimately responsible for the payment of principal and interest when due. Subsequent to July 1, 1979, the Authority has issued only special obligation bonds for which principal and interest is solely payable from the revenues of the institutions and is not a debt of the Authority or the State of Connecticut. As of June 30, 2011, there were no general obligation bonds outstanding. The state is not obligated for the debt, except for debt that is issued under the Child Care Facilities Loan Program and the Special Capital Reserve Program.

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

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

The Authority provides grants to non-profit organizations that provide essential health, educational, cultural, and childcare services to Connecticut residents in targeted geographic areas of Connecticut. The awarding of new grants under the Client and Open Grant Programs was temporarily suspended during fiscal years ended June 30, 2009 and June 30, 2010 due to the Authority's participation in the state's Deficit Mitigation Plan, which required a \$13,150,000 transfer to the State of Connecticut. During the fiscal year ended June 30, 2011, CHEFA's Open Grant and Client Grant Programs were reinstated.

**Board of Directors and Administrative Officials:**

Pursuant to Section 10a-179(a) of the General Statutes, the Authority operates under a ten person board of directors. The board of directors includes the State Treasurer and the Secretary of the Office of Policy and Management as ex-officio members and eight residents of the state who are appointed by the Governor. Not more than four of the eight members appointed by the Governor can be of the same political party. In addition, three appointed members shall be trustees, directors, officers or employees of institutions for higher education, two appointed members shall be trustees, directors, officers or employees of healthcare institutions and one shall be a person having a favorable reputation for skill, knowledge, and experience in state and municipal finance. Members of the board of directors as of June 30, 2011, were as follows:

Ex-Officio:

Denise L. Nappier, State Treasurer (Sarah K. Sanders, designated representative)  
Benjamin B. Barnes, Office of Policy and Management (Robert S. Dakers, designated representative)

Appointed by the Governor:

Barbara Rubin, Chairperson  
Patrick A. Colangelo, Vice Chairperson  
Dr. Estela R. Lopez  
John M. Biancamano  
Paul Mutone  
Peter W. Lisi  
Benson R. Cohn  
Bryan K. Pollard, Esq.

The executive director of the Authority is appointed by the board of directors. Jeffrey A. Asher served in that capacity throughout the audited period.

**Significant State Legislation:**

Public Act 10-75, among other things, provides loan reimbursements and grants to Connecticut students seeking jobs in alternative energy technology and other related fields by transferring \$3 million from the quasi-public Connecticut Health and Educational Authority to the General Fund.

**Accounting Policies:**

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

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

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

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

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

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

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

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

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

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

**Special Capital Reserve Funds** – These funds are maintained to ensure compliance with minimum capital reserve requirements of bond issues. Any deficiencies in the reserves are required to be funded by the institution after notification by the trustee. If the bond was issued

under Section 10a-186a of the General Statutes, the state is obligated to replenish the fund if the institution does not.

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

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

**RÉSUMÉ OF OPERATIONS:**

The financial position of the Authority as of June 30, 2010 and 2011, per its audited financial statements, is presented below.

	<u>As of June 30,</u>	
	<u>2011</u>	<u>2010</u>
Assets		
Current Assets:		
Unrestricted Assets:		
Cash	\$ 240,000	\$ 351,000
Accounts Receivable, Net of Allowance for Bad Debt	200,000	191,000
Investments	7,189,000	5,432,000
Prepaid Expenses and Other	<u>120,000</u>	<u>131,000</u>
Total Unrestricted Assets	<u>7,749,000</u>	<u>6,105,000</u>
Restricted Assets:		
Cash	36,000	42,000
Fund Investments	358,361,000	445,584,000
Other Investments	6,037,000	6,036,000
Interest Receivables	49,000	103,000
Other Receivables	<u>0</u>	<u>1,000</u>
Total Restricted Assets	<u>364,483,000</u>	<u>451,766,000</u>
Total Current Assets	<u>372,232,000</u>	<u>457,871,000</u>
Noncurrent Assets:		
Investments (Restricted)	10,580,000	10,040,000
Capital Asset, Net of Depreciation	<u>188,000</u>	<u>271,000</u>
Total Noncurrent Assets	<u>10,768,000</u>	<u>10,311,000</u>
<b>Total Assets</b>	<b><u>\$ 383,000,000</u></b>	<b><u>\$ 468,182,000</u></b>

**Liabilities and Net Assets**

Current Liabilities:

Accounts Payable and Accrued Expenses	\$ 4,181,000	\$ 1,007,000
Amounts Held for Institutions	<u>364,483,000</u>	<u>451,766,000</u>
Total Current Liabilities	368,664,000	452,773,000

Noncurrent Liabilities:

Amount Held on Behalf of State of CT	<u>2,207,000</u>	<u>2,220,000</u>
Total Liabilities	<u>370,871,000</u>	<u>454,993,000</u>

Net Assets:

Invested in Capital Assets	188,000	271,000
Restricted	5,373,000	7,820,000
Unrestricted	<u>6,568,000</u>	<u>5,098,000</u>
Total Net Assets	<u>12,129,000</u>	<u>13,189,000</u>

**Total Liabilities and Net Assets**            **\$383,000,000**            **\$ 468,182,000**

The Authority invests any excess funds in short-term investments and marketable securities, including the State Treasurer's Short Term Investment Fund (STIF) to earn investment income.

As of June 30, 2011, the Authority holds \$10,580,000 in reserves; \$2,207,000 on behalf of the State of Connecticut to guarantee loans pursuant to Sections 17b-749g and 17b-749h of the General Statutes and \$8,373,000 from the Authority's reserve funds pursuant to Public Acts 97-259, 09-110, and 10-75. Section 17b-749g established the Guaranteed Loan Fund Program and Section 17b-749h established the Small Direct Revolving Loan Program. The state provided \$1.5 million and \$750,000, respectively, to fund loan guarantees made under the programs. To date, there have been four calls on loans guaranteed under the Small Direct Revolving Loan Program for a loss of \$43,000. Funds held on behalf of the State of Connecticut are invested in the State Treasurer's Short Term Investment Fund (STIF). The Authority also has a reserve of \$4,320,000 for the School Readiness and Child Daycare Guaranteed Loan Fund Program pursuant to Public Act 97-259, \$1,053,000 pursuant to Public Act 09-110 for the purpose of guaranteeing qualifying student loans under the Credit Union League of Connecticut Student Loan Program, and \$3,000,000 for the Connecticut Green Technology, Life Science, and Health Information Technology Loan Forgiveness Program, pursuant to Public Act 10-75.

Fund investments are investments associated with construction and project funds that are managed and held by the Authority on behalf of client institutions. Decreases in fund investments during the fiscal year ended June 30, 2011, reflect the net effects of disbursement of funds.

A statement of revenues, expenses and changes in net assets for the fiscal years ended June 30, 2010 and 2011, follows. The information was obtained from the Authority's audited financial statements.

	<u>As of June 30,</u>	
	<u>2011</u>	<u>2010</u>
Operating Revenues:		
Revenues from Institutions:		
Administrative Fees	\$6,687,000	\$ 6,247,000
Bond Issuance Fees	97,000	67,000
Miscellaneous Revenues	<u>4,000</u>	<u>23,000</u>
Total Operating Revenues	<u>6,788,000</u>	<u>6,337,000</u>
Operating Expenses:		
Salaries and Related Expenses	2,722,000	2,685,000
Other Operating Expenses	<u>1,163,000</u>	<u>1,283,000</u>
Total Operating Expenses	<u>3,885,000</u>	<u>3,968,000</u>
Operating Income (Loss)	2,903,000	2,369,000
Non-Operating Revenues (Expenses):		
Income from Investments	22,000	<u>32,000</u>
Grant Expense	<u>(985,000)</u>	-
Change in Net Assets	1,940,000	2,401,000
Capital Transfers:		
Transfer to the State of Connecticut	<u>(3,000,000)</u>	-
Increase/(decrease) in Net Assets	(1,060,000)	2,401,000
Net Assets, Beginning of Year	<u>13,189,000</u>	<u>10,788,000</u>
<b>Net Assets, End of Year</b>	<b><u>\$ 12,129,000</u></b>	<b><u>\$ 13,189,000</u></b>

Total revenues for the fiscal year ended June 30, 2010, and 2011 were \$6,369,000 and \$6,810,000, respectively. For comparison purposes, total revenue for the fiscal year ended June 30, 2009 totaled \$7,368,000. The reduction in total revenue is attributable to reduced miscellaneous revenues and income from investments during the fiscal years audited, over fiscal year ended June 30, 2009. The Authority charges an annual administrative fee to institutions with outstanding bond issues to cover operating expenses of the Authority. All issues other than those under the Special Capital Reserve Program are charged an annual fee of nine basis points on the outstanding par amount of the bonds. Bonds issued under the Special Capital Reserve Program are charged an annual fee of fourteen basis points. The increase in fee revenue reflects the impact of new issuances and the par amount of bonds outstanding. The Authority also charges a bond issuance fee of \$5,000 for each bond issue.

Income from investments fell during the fiscal year ended June 30, 2010 and 2011 over 2009 levels, due to a decline in general market rates as well as a decline in the amount invested.

Operating expenses of the Authority totaled \$3,968,000 and \$4,870,000 during the fiscal year ended June 30, 2010, and 2011, respectively. For comparison purposes, operating expenses for the fiscal year ended June 30, 2009 totaled \$5,546,000. The Authority's operating expenses consist of salary, other expenses, grant expense, and other operating expenses. Operating expenses decreased in fiscal year ended June 30, 2010 from fiscal year ended June 30, 2009 levels by \$1,578,000 reflecting, for the most part, the complete suspension of grant programs during that fiscal year. Operating expenses increased in fiscal year ended June 30, 2011 by \$902,000, over fiscal year ended June 30, 2010 levels, primarily representing the resumption of the grant program during that fiscal year.

The transfer of \$3 million to the State of Connecticut is in accordance with Public Act 10-75, as noted in the Significant State Legislation section of this report.

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**CONDITION OF RECORDS**

**Bond Application Not on File:**

*Criteria:* Section 10a-179(h) of the General Statutes requires that the board of directors of the Authority adopt written procedures for awarding loans, grants and other financial assistance.

Section 1-126 of the General Statutes mandates that any quasi-public agency shall require any application, agreement, financial statement, certificate or other writing submitted to them that provides information on which the decision of such quasi-public agency was based, to be signed under penalty of false statement as provided in Section 53a-157b of the General Statutes.

Lastly, the procedures of the Connecticut Health and Educational Facilities Authority (CHEFA) stipulate that, “each entity that requests the Authority to issue bonds...shall make application to the Authority in such form and manner as the staff shall determine.”

*Condition:* An application letter to support a client’s request for bond financing in the amount of \$132,990,000 could not be located for one out of ten issues tested.

*Effect:* The various statutory and procedural requirements intrinsic to the bond issuance process cannot be documented without an application on file.

*Cause:* According to the Authority, the application appears to have been misplaced or misfiled.

*Recommendation:* The Connecticut Health and Educational Facilities Authority should strengthen its internal controls to ensure that a valid application is obtained and on file for every bond issuance. (See Recommendation 1).

*Agency Response:* “With regard to the Application Letter for the above referenced client institution, the Authority received the \$20,000 Application Fee on April 10, 2010 and believed at that time that the signed Application Letter had accompanied the check, which is typically the case for every bond issue. Therefore, we believe that the letter was misfiled or misplaced.

Measures taken to ensure the timely receipt of the Application Letter and properly filing the letter include 1) following up with the client institution prior to the Board meeting in which the bond issue will be approved; 2) tracking receipt of the Application letters on the Authority’s internal master bond financing schedule; and 3) once a hard copy is received, maintaining the letter in the permanent file and scanning the letter to be stored electronically on the data base system for the bond issue.”

**RECOMMENDATIONS**

*Status of Prior Audit Recommendations:*

Our prior audit examination resulted in one recommendation. The following is a summary of that recommendation and action taken by the Authority.

- The Connecticut Health and Educational Facilities Authority should strengthen internal control by enforcing current policies to ensure compliance in all areas of business operations. We found continued issues with loan applications not on file; accordingly, we are repeating this recommendation in revised form.

*Current Audit Recommendation:*

- 1. The Connecticut Health and Educational Facilities Authority should strengthen its internal controls to ensure that a valid application is obtained and on file for every bond issuance.**

Comment:

An application letter to support a client's request for bond financing, in the amount of \$132,990,000, could not be located for one out of ten issues tested.

## INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 and Section 1-122 of the General Statutes, we have conducted an audit of the State of Connecticut Health and Educational Facilities Authority's operations for the fiscal years ended June 30, 2010 and 2011. This audit was primarily limited to performing tests of the Authority's compliance with certain provisions of laws, regulations, contracts and grant agreements, including but not limited to a determination of whether the Authority has complied with its regulations concerning affirmative action, personnel practices, the purchase of goods and services, the use of surplus funds and the distribution of loans, grant agreements and other financial resources, and to understanding and evaluating the effectiveness of the Authority's internal control policies and procedures for ensuring that the provisions of certain laws, regulations, contracts and grant agreements applicable to the Authority are complied with. The financial statement audit of the State of Connecticut Health and Educational Facilities Authority for the fiscal years indicated above, was conducted by the Authority's independent public accountants.

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

### **Internal Control over Compliance:**

Management of the State of Connecticut Health and Educational Facilities Authority is responsible for establishing and maintaining effective internal control over its operations. In planning and performing our audit, we considered the State of Connecticut Health and Educational Facilities Authority's internal control over its operations as a basis for designing our auditing procedures for the purpose of evaluating the Authority's operations and compliance with certain provisions of laws, regulations, contracts and grant agreements, but not for the purpose of expressing an opinion the effectiveness of the Authority's internal control over operations and compliance. Accordingly we do not express an opinion.

Our consideration of internal control included, but was not limited to, the following areas:

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, unauthorized, illegal, or irregular transactions on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control that

adversely affects the Authority's ability to properly initiate, authorize, record, process, or report data reliably consistent with management's direction, and/or comply with certain provisions of laws, regulations, contracts, and grant agreements such that there is a reasonable possibility that material compliance with laws, regulations, contracts and grant agreements will not be prevented or detected and corrected on a timely basis.

Our consideration of the internal control over the Authority's operations was for the limited purpose described previously and was not designed to identify all deficiencies in the internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies that we consider to be material weaknesses, as defined previously.

**Compliance and Other Matters:**

As part of obtaining reasonable assurance about whether the State of Connecticut Health and Educational Facilities Authority complied with laws, regulations, contracts and grant agreements, noncompliance with which could result in significant unauthorized, illegal, irregular or unsafe transactions or could have a direct and material effect on the results of the Authority's operations for the fiscal years ended June 30, 2010 and 2011, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, including but not limited to the following areas:

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

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

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

The State of Connecticut Health and Educational Facilities Authority's response to the findings identified in our audit are described in the accompanying Condition of Records section of this report. We did not audit the Authority's response and, accordingly, we express no opinion on it.

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

regulations, contracts and grant agreements included within the scope of this audit.

**CONCLUSION**

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



Gary Kriscenski  
Principal Auditor

Approved:



John C. Geragosian  
Auditor of Public Accounts



Robert M. Ward  
Auditor of Public Accounts