

STATE OF CONNECTICUT



*AUDITORS' REPORT
CONNECTICUT HOUSING FINANCE AUTHORITY FOR THE CALENDAR YEARS
ENDED DECEMBER 31, 2010 AND 2011*

AUDITORS OF PUBLIC ACCOUNTS
JOHN C. GERAGOSIAN ❖ ROBERT M. WARD

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July 24, 2013

AUDITORS' REPORT CONNECTICUT HOUSING FINANCE AUTHORITY FOR THE CALENDAR YEARS ENDED DECEMBER 31, 2010 AND 2011

We have examined the books, records, and accounts of the Connecticut Housing Finance Authority (CHFA), as provided in Section 2-90 and Section 1-122 of the General Statutes, for the calendar years ended December 31, 2010 and 2011. Included in this examination is the State Housing Authority (SHA), a subsidiary of CHFA, established in accordance with Section 8-244b of the General Statutes.

SCOPE OF AUDIT:

This audit was primarily limited to performing tests of CHFA's compliance with certain provisions of laws, regulations, contracts, and grants, including but not limited to a determination of whether CHFA has complied with its regulations concerning the following areas:

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

Our audit included an examination of a representative sample from the fiscal years under review of the authority's activities in the areas identified above, as well as other areas we deemed necessary. We also considered the authority's internal control over its operations in these same areas that could have a significant effect on its operations and for the purposes of evaluating compliance with certain provisions of laws, regulations, contracts and grants. However, the purpose of this examination was not to provide assurance on the internal control over those areas of operations.

The financial statement audits of the authority for the fiscal years ended December 31, 2010 and 2011 were conducted by the authority's independent public accountants. This report on our examination consists of the Comments, Condition of Records, and Recommendations which follow.

COMMENTS

FOREWORD:

The Connecticut Housing Finance Authority operates under the provisions of Chapter 134, Sections 8-241 through 8-265ss of the General Statutes. It was established during the 1972 session of the General Assembly as the successor to the Connecticut Mortgage Authority, which had been established by the General Assembly in 1969. CHFA is a body politic and corporate, constituting a public instrumentality and political subdivision of the state. It was created to alleviate the shortage of housing for low-income and moderate-income families, and to encourage the development of a balanced community of all income levels in the urban areas. In accordance with Section 8-244b of the General Statutes, CHFA established the State Housing Authority, which is a subsidiary of CHFA.

Funds to finance mortgage loans are primarily obtained by issuing bonds, the interest from which has generally been exempt from federal income tax to the bondholder. Loans made from the proceeds of bonds are secured by a first mortgage lien. Funds derived from the excess of interest income from loans over bond interest expenses are used to pay CHFA's operating expenses.

BOARD OF DIRECTORS AND ADMINISTRATIVE OFFICIALS:

In accordance with Section 8-244 subsection (a) of the General Statutes, the governing body of the authority consists of 15 directors. Four directors are ex-officio members, seven members are appointed by the Governor, and four are appointed by the General Assembly. Members of the CHFA board of directors as of December 31, 2011, were as follows:

Ex-officio members:

Catherine Smith	Chairperson Commissioner, Dept. of Economic and Community Development
Denise L. Nappier	State Treasurer
Howard F. Pitkin	Banking Commissioner
Benjamin Barnes	Secretary, Office of Policy and Management

Appointed members:

- Orest T. Dubno, Vice Chairperson
- Jeffrey Freiser
- J. Scott Guilmartin
- Kimberly A. Neilson
- Barbara McGrath
- Meghan K. Lowney
- Michael Lyons
- 4 Vacancies

Two of the vacancies occurred during the 2011 calendar year; one member stepped down in February 2011 and the other in December 2011. The third vacancy has existed since July 2009 and the fourth vacancy has existed since June 2007.

Timothy Bannon served as president/executive director until January 5, 2011, at which time Susan Whetstone was appointed to the post on an interim basis and served through the remainder of the audited period.

In accordance with Section 8-244b subsection (a) of the General Statutes, the governing body of the State Housing Authority consists of three members appointed by the board of directors of CHFA. Members of the State Housing Authority board of directors as of December 31, 2011, were as follows:

Catherine Smith	Chairperson
Michael Lyons	
Barbara McGrath	

NEW LEGISLATION:

Public Act 10-172 changed the requirements for compliance audits of quasi-public agencies to be performed on a biennial rather than annual basis, effective July 1, 2010.

Public Act 11-140 states that the chairperson of the CHFA board shall be the Commissioner of Economic and Community Development.

CHFA PROGRAMS:

CHFA provides housing-related financing through several programs at interest rates below those generally available. Programs include Downpayment Assistance, Police Homeownership, Military Homeownership, Teacher Mortgage Assistance, and the Assisted Living Demonstration Pilot Program. Financing programs are divided into two general categories, single-family housing and multi-family housing.

Single-Family Housing:

CHFA provides financing to low and moderate-income households to help create affordable housing opportunities. Single-family homes, condominiums and qualified mobile homes may be financed. The authority's homebuyer mortgage funds are distributed through participating lenders and are generally available for a maximum of 30 years.

The authority adopts limitations for eligibility in its home mortgage programs. Limitations include sales price and family income, and vary based on geographical areas within the state.

The authority requires the homeowner to occupy and use the residential property for a permanent, primary residence within 60 days of the closing of the mortgage loan. Various other criteria related to both borrower eligibility and property eligibility are contained in the *Procedures of the Connecticut Housing Finance Authority*.

The authority also operates an Urban Area Mortgages Program for home mortgages. Under this program, the authority may finance mortgage loans in certain state and federally designated urban targeted areas with fewer restrictions on the borrower's income. Applications under this program are considered only when conventional loans are not available.

Multi-Family Housing:

Multi-family mortgage loans provide permanent financing for the construction of new, or rehabilitation of pre-existing, multi-family projects. Increasing the supply and availability of affordable housing for low and moderate-income households is the primary role of CHFA. By offering financing terms not generally available in the commercial market, the authority can help developers achieve feasibility for projects which otherwise would not be possible.

Projects eligible for financing under this program may be designated for individuals, families, the elderly, or people with special needs. Projects must contain a minimum of 25 units, while smaller projects may be considered for non-profit organizations. Federal tax credits are available to developers under this plan provided that certain set-aside requirements related to tenant income are met.

There is a Multi-Family Housing Underwriting Unit that underwrites the financing of multi-family rental housing developments, providing direct construction and/or permanent mortgage loans to private developers and not-for-profit sponsors for construction or rehabilitation of rental housing. The staff reviews loan proposals, analyzes sites and financial statements, and performs feasibility analyses to determine a proposal's acceptability. The Multi-Family Technical Services staff ensures that plans and specifications meet authority standards and construction proceeds are disbursed according to approved plans and timetables, approves budget changes, and observes the integrity of developments. The unit also verifies projected costs, reviews appraisals for accuracy and completeness, and administers the State of Connecticut Low Income Housing Tax Credits by monitoring unit compliance and tenant eligibility.

Section 8-251 subsection (a) of the General Statutes currently permits the authority to purchase or make \$1,500,000,000 of mortgage loans for single-family or multi-family housing programs, which are uninsured or not guaranteed by a federal agency, a federally chartered corporation, a private mortgage insurance company, the state or the authority itself. The authority had financed or firmly committed to finance approximately \$1,100,930,000, or 73 percent, of the allowable maximum of such mortgage loans as of December 31, 2010 and \$1,140,796,000, or 76 percent, of the allowable maximum of such mortgage loans as of December 31, 2011.

RÉSUMÉ OF OPERATIONS:

During the calendar years ended December 31, 2010 and 2011, the authority maintained three funds in accordance with the provisions of Section 8-258 of the General Statutes: the Housing Mortgage Capital Reserve Fund, the Housing Mortgage General Fund, and a Housing Mortgage Insurance Fund. In addition, the authority maintained Special Needs Housing Funds, including a Capital Reserve Fund, a Special Needs Housing Renewal and Replacement Fund,

and Housing Draw Down Funds, including Bond Escrow Fund and the Rebate Fund. During the audited period, CHFA assets also consisted of various component units created to hold foreclosed real estate. As previously noted, we did not audit these funds since they were already audited by an independent public accounting firm. We rely on the opinion expressed by the independent public accountants. The following information includes general data about funds associated with CHFA. More detailed financial data concerning these funds can be found in the authority's annual reports.

Housing Mortgage Capital Reserve Fund:

In accordance with Section 8-258 subsection (a)(1) of the General Statutes, the Housing Mortgage Capital Reserve Fund shall maintain an amount of money sufficient to meet the principal and interest payments on outstanding bonds required in the succeeding calendar year. This fund consists of proceeds from the sale of bonds that are required to be deposited into this account by the bond resolution. Also included in this fund are other monies available to the authority that it can utilize for this purpose. This fund would only be used to pay bond principal and interest if there were insufficient funds within the Housing Mortgage General Fund.

Housing Mortgage General Fund:

The Housing Mortgage General Fund was established pursuant to Section 8-258 subsection (a)(3) of the General Statutes to account for any monies not required to be deposited into the Housing Mortgage Capital Reserve Fund or allocated to any other fund, including proceeds from the sale of bonds. This fund is used to pay all operating costs, including payments of principal and interest on the bonds issued by the authority. No appropriations have been made by the General Assembly for the general operations of the authority with the exception of the initial appropriation made in the 1969-1970 fiscal year. The state provides services to CHFA for the processing of payroll and related employee benefits. During the calendar years ended December 31, 2010 and 2011, CHFA wired \$17,474,033 and \$17,466,184, respectively, to the Office of the State Treasurer to provide for all such payroll and payroll processing costs.

Housing Mortgage Insurance Fund:

In accordance with Section 8-258 subsection (a)(4) of the General Statutes, CHFA is authorized to establish a Housing Mortgage Insurance Fund. This fund shall consist of mortgage insurance premium receipts; money or assets received from loan defaults or delinquencies (including sales, lease or rental of real property); monies lent or paid by the state for inclusion in this fund; and any other monies available to the authority that it can include therein. Payments for expenses related to the protection of the authority's interest in connection with delinquent or defaulted insured mortgages shall be made from this fund. Loans and advances may be made from said funds as provided by Section 8-250 of the General Statutes.

Statement of Net Position (thousands of dollars):

Assets	As of December 31,		
	2011	2010	2009
Mortgage Loans Receivable	\$ 3,606,571	\$ 3,552,918	\$ 3,373,682
Investments in Securities ⁽¹⁾	1,651,022	1,658,234	1,617,683
Deferred Outflows of Resources ⁽²⁾	232,719	153,434	
All Other Assets	133,672	117,951	327,454
Total Assets and Deferred Amounts	5,623,984	5,482,537	5,318,819
Liabilities			
Bonds Payable	4,160,630	4,134,969	4,189,023
Escrow Deposits	218,309	233,341	187,560
All Other Liabilities	287,324	210,331	61,253
Total Liabilities	4,666,263	4,578,641	4,437,836
Net Position	\$ 957,721	\$ 903,896	\$ 880,983

(1) Investments in securities include capital reserve funds of \$912,031, \$780,853, and \$777,673 in the 2009, 2010, and 2011 audited years, respectively.

(2) The authority adopted Governmental Accounting Standards Board Statement (GASB) No. 53, *Accounting and Financial Reporting for Derivative Instruments*, which required reporting of the deferred outflows of resources category effective January 1, 2010.

In accordance with GASB No. 53, the authority began reporting deferred outflows of resources for its derivative financial instruments for the year ended December 31, 2010. The authority has entered into interest rate swap agreements, derivative instruments, which are structured for the authority to pay a fixed interest rate while receiving variable interest rates from the swap counterparty. Based on future value estimations, the authority's interest rate swaps have a reported fair value loss of \$232,719,000, as of December 31, 2011.

Statement of Revenues, Expenses and Changes in Net Position (thousands of dollars)

	2011	2010	2009
Operating Revenues			
Interest on Mortgage Loans	\$ 199,516	\$ 188,669	\$ 180,589
Interest on Investments	38,389	44,624	55,566
Fees and Other Income	11,138	6,079	7,242
Total Operating Revenues	249,043	239,372	\$ 243,397
Operating Expenses			
Interest	160,754	177,735	\$188,307
Amortization of Deferred Financing Costs	6,718	8,565	5,351
Servicer Fees	8,359	8,429	8,736
Administrative	35,067	34,816	34,769
Provision for Losses	14,682	7,289	1,728
Total Operating Expenses	225,580	236,834	238,891
Operating Income	23,463	2,538	4,506

Non-Operating Revenues (Expenses)	2011	2010	2009
Net Increase (Decrease) in the Fair Value of Investments ⁽¹⁾	27,163	26,650	(18,091)
State and Federal Program Funding	28,239	67,019	18,630
State and Federal Program Expenses	(25,040)	(73,294)	(12,953)
Non-Operating Income	30,362	20,375	(12,414)
Change in Net Position	53,825	22,913	(7,908)
Net Position, Beginning of Year	903,896	880,983	888,891
Net Position, End of Year	\$ 957,721	\$ 903,896	\$ 880,983

⁽¹⁾ Includes the real estate owned line item presented in the 2009 audited financial statements.

Connecticut Housing Finance Authority Bonds:

In accordance with the provisions of Section 8-250 subsection (12) and Section 8-252 of the General Statutes, the authority is authorized to issue bonds as necessary to provide sufficient funds for carrying out the purposes of the authority. Bonds issued by the authority have generally been tax-exempt. The tax-exempt bonds are not backed by the full faith and credit of the State of Connecticut. However, the state, on or before December 1st of each year, must appropriate from the General Fund whatever amount is certified by the chairman of the authority as necessary to restore the Capital Reserve Fund to the required minimum capital reserve. The General Fund has not been used to fund the Capital Reserve Fund during the audited period.

The amounts on deposit in the Bond Resolution Capital Reserve Fund were \$775,339,000 on December 31, 2010 and \$772,001,000 on December 31, 2011; which was in excess of the Bond Resolution Capital Reserve Fund minimum requirements of \$292,254,000 and \$279,202,000, respectively. The amounts on deposit in the Indenture Capital Reserve Fund were \$5,514,000 on December 31, 2010 and \$5,672,000 on December 31, 2011; which was in excess of the Indenture Capital Reserve Fund minimum requirements of \$4,260,000 and \$4,590,000, respectively. For both of these capital reserve funds, the minimum is the amount of debt service due in the following year and the maximum is the greatest amount of debt service due in any succeeding year. The authority generally issues two types of bonds; the Housing Mortgage Finance Program Bonds and the Special Needs Housing Mortgage Finance Program Bonds. The table below illustrates the changes in bonds payable for the years ended December 31, 2010 and December 31, 2011.

Change in Bonds Payable (thousands of dollars):

Types of Program Bonds:	Balance at 12/31/09	Additions⁽²⁾	Reductions⁽³⁾	Balance at 12/31/10
Housing Mortgage Finance ⁽¹⁾	\$3,914,223	\$575,900	(\$708,026)	\$3,782,097
Special Needs Mortgage Finance	55,470	28,095	(17,155)	66,410
Single Family Special Obligation	191,720	66,670	0	258,390
Multifamily Special Obligation	27,610	0	0	27,610
	\$4,189,023	\$670,665	(\$725,181)	\$4,134,507

	Balance at 12/31/10	Additions⁽²⁾	Reductions⁽³⁾	Balance at 12/31/11
Housing Mortgage Finance ⁽¹⁾	\$3,782,097	\$533,792	(\$616,147)	\$3,699,742
Special Needs Mortgage Finance	66,410	0	(1,130)	65,280
Single Family Special Obligation	258,390	106,330	(1,815)	362,905
Multifamily Special Obligation	27,610	0	0	27,610
	\$4,134,507	\$640,122	(\$619,092)	\$4,155,537

⁽¹⁾ Includes Housing Mortgage Finance Program Other Bonds.

⁽²⁾ Additions include new issues and accreted interest.

⁽³⁾ Reductions include retirements and refunded bonds.

Investments:

In accordance with Section 8-258 subsection (c) and Section 8-250 subsection (18) of the General Statutes, CHFA shall invest any funds not needed for immediate use or disbursement, including any funds held in reserve. The nature of such investments is limited to obligations issued or guaranteed by the United States of America or the State of Connecticut and other obligations that are legal investments for savings banks in this state and time deposits or certificates of deposit or similar type investments as determined by the authority. The authority's investments were valued at \$1,658,234,000 on December 31, 2010 and \$1,651,022,000 on December 31, 2011, including \$780,853,000 and \$777,673,000 in capital reserve funds for the respective audited years. Interest earnings on investments totaled \$44,624,000 for the year ended December 31, 2010 and \$38,389,000 for the year ended December 31, 2011.

Staffing Levels:

The number of employees as of December 31, 2009 and December 31, 2010, was 125 and 132, respectively, an increase of 5.6 percent. The number of employees as of December 31, 2011 was 129, a decrease of 2.3 percent.

Personal services costs, including fringe benefits, decreased by about \$850,000, or five percent, for 2010 and remained about equal in 2011.

Other Examinations:

CHFA has been subject to annual audits by independent public accountants covering its financial operations, loan processing functions, and the Section 8 federally assisted housing payments program under the United States Housing Act of 1937. The independent public accountant's report to CHFA dated May 16, 2011 for the year ended December 31, 2010, expressed an unqualified opinion on CHFA's financial statements and reported no material weaknesses in internal control. The independent public accountant's report to CHFA dated April 26, 2012 for the year ended December 31, 2011, expressed an unqualified opinion on CHFA's financial statements and reported no material weaknesses in internal control.

CONDITION OF RECORDS

Our examination of the records of the authority disclosed the following matters of concern requiring attention.

Contract Execution:

Criteria: Section D-2 of the CHFA Purchasing Procedures requires contracts for the purchase of goods and services with a value greater than \$10,000.

The following affidavits are required by Connecticut General Statutes (CGS) for all contracts in excess of \$50,000:

1. Gift/Campaign Contribution (CGS Section 4-252)
2. Consulting (CGS Section 4a-81)
3. Nondiscrimination and affirmative action (CGS Section 4a-60)

Sound business practice dictates that required contracts and affidavits are fully executed prior to the commencement of services.

Condition: Our review disclosed one instance in which work commenced about 10 months prior to the execution of a contract. Between the commencement of work in September 2010 and the execution of the contract in July 2011, about \$33,000 of charges had accrued for the project, which had an expected total value of about \$77,000.

Effect: CHFA was not in compliance with their purchasing procedures and statutory requirements concerning procurement of services. Not having a fully executed contract prior to the commencement of work increases risk of disputes over the scope of services to be provided and associated costs.

Cause: Agency oversight allowed for the deviation from established purchasing procedures.

Recommendation: CHFA should ensure that established contracting procedures are followed and that contracts are fully executed prior to the delivery of goods or commencement of services.

Agency Response: “The authority agrees that in this instance it was not in compliance with its purchasing procedures and statutory requirements concerning procurement of services due to an oversight in its continuation of a prior contractual relationship.

The necessary contract and statutory requirements have been obtained and the authority is developing improved procedures and monitoring processes regarding timely execution of its contracts.”

RECOMMENDATIONS

Status of Prior Audit Recommendations:

Our prior audit did not contain any recommendations.

Current Audit Recommendations:

- 1. CHFA should ensure that established contracting procedures are followed and that contracts are fully executed prior to the delivery of goods or commencement of services.**

Comments:

The current review noted an instance in which work had commenced prior to the execution of the required contract and statutorily required affidavits.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 and Section 1-122 of the General Statutes, we have conducted an audit of the Connecticut Housing Finance 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 audits of the Connecticut Housing Finance Authority, for the fiscal years indicated above, were 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 Connecticut Housing Finance 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 Connecticut Housing Finance Authority is responsible for establishing and maintaining effective internal control over its operations. In planning and performing our audit, we considered the Connecticut Housing Finance 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 on 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 noncompliance 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 in internal control that we consider to be material weaknesses, as defined previously

Compliance and Other Matters:

As part of obtaining reasonable assurance about whether the Connecticut Housing Finance 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 year 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 operations in those areas and performing such other procedures as we considered necessary in the circumstances.

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

The Connecticut Housing Finance Authority's response to the findings identified in our audit is 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 and use 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 courtesies and cooperation extended to our representatives by the personnel of the Connecticut Housing Finance Authority during the course of our examination.



Douglas Stratoudakis
Auditor II

Approved:



John C. Geragosian
Auditor of Public Accounts



Robert M. Ward
Auditor of Public Accounts