

STATE OF CONNECTICUT



*AUDITORS' REPORT
CONNECTICUT INNOVATIONS, INCORPORATED
FOR THE FISCAL YEAR ENDED JUNE 30, 2007*

AUDITORS OF PUBLIC ACCOUNTS

KEVIN P. JOHNSTON ❖ ROBERT G. JAEKLE

Table of Contents

INTRODUCTION	1
SCOPE OF AUDIT	1
COMMENTS	2
FOREWORD	2
Significant State Legislation.....	5
Board of Directors and Administrative Officials.....	5
RÉSUMÉ OF OPERATIONS:	6
State Accounts	7
Connecticut Innovations Incorporated Accounts.....	7
Connecticut Clean Energy Fund.....	10
Other Examinations	14
CONDITION OF RECORDS	15
Connecticut Clean Energy Fund Revenues.....	15
Conflicting Statutory Reporting Provisions.....	16
Investments	17
Personnel Policies – Time and Attendance.....	19
Personnel Policies – Telecommuting.....	21
RECOMMENDATIONS	23
CERTIFICATION	25
CONCLUSION	28

October 22, 2008

**AUDITORS' REPORT
CONNECTICUT INNOVATIONS, INCORPORATED
FOR THE FISCAL YEAR ENDED JUNE 30, 2007**

We have made an examination of the financial records of the Connecticut Innovations, Incorporated (the Corporation), as provided in Section 2-90 and Section 1-122 of the General Statutes, for the fiscal year ended June 30, 2007.

SCOPE OF AUDIT:

This audit was primarily limited to performing tests of the Corporation's compliance with certain provisions of laws, regulations, contracts and grants, including but not limited to, a determination of whether the Corporation has complied with its written operating procedures, that are required per Section 32-35 (d) of the General Statutes, concerning the following areas:

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

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

Our audit included a review of a representative sample of the Corporation'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 Corporation for the fiscal year indicated above, was

conducted by the Corporation's independent public accountants.

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

COMMENTS

FOREWORD:

Connecticut Innovations, Incorporated (hereafter CI or the Corporation) operates primarily under Chapter 581, Sections 32-32 through 32-47a of the General Statutes. Pursuant to Section 32-35 of those Statutes, it is a public instrumentality and political subdivision of the State. During the audit period the Corporation was also responsible for administering the Renewable Energy Investment Fund, commonly referred to as the Connecticut Clean Energy Fund (CCEF), as required under Section 16-245n of the General Statutes. Pursuant to Chapter 12 of the General Statutes, it is classified as a quasi-public agency and therefore is subject to the requirements related to such agencies as may be found in Chapter 12. As a quasi-public agency, the Corporation's financial information is included as a component unit in the State of Connecticut's Comprehensive Annual Financial Report (CAFR).

CI was established to stimulate and encourage the research and development of new technologies and new products, the development and operation of science parks and incubator facilities, and to promote science, engineering, mathematics and other disciplines essential to the development of technology.

The Corporation provides financial assistance to Connecticut businesses for the development and marketing of high-technology products, services, and processes. This assistance has been made in the form of loans, royalty agreements and equity (ownership) investments. The Corporation also funds other organizations such as Connecticut universities and technology research or application centers. The Corporation includes contingent payback provisions to those funds as a means of sharing in the royalties and other earnings from successful research projects.

The Corporation targets early stage high-technology enterprises. These include: advanced materials, aerospace, biotechnology, energy and environmental systems, information technology and photonics. To address these areas the Corporation utilizes a number of limited partnerships and financial investments to achieve its objectives of assisting qualified Connecticut organizations.

The Corporation provides several financial and technical programs to assist qualifying Connecticut companies, colleges and universities. These include:

Access Connecticut Limited Partnership – This program is a limited partnership designed to generate new technology companies in Connecticut through technology transfer from universities.

Connecticut Emerging Enterprise Limited Partnership – This program is a partnership between the Corporation and a major commercial bank. The program invests in initial and

follow-on rounds of financing for early stage, technology growth enterprises with significant proprietary innovations or other unique, sustainable competitive advantages.

Connecticut Innovations Technology Scholars Program – This program provides scholarships to encourage talented young people to choose careers in science and technology and to pursue their education and their careers in Connecticut.

Eli Whitney Investments – This is the Corporation’s primary investment program. The program makes risk capital investments in emerging and established companies to stimulate their development of high technology products, processes and services. Areas of focus include bioscience, energy and environmental systems, information technology, photonics/applied optics, advanced materials and engineering.

Next Generation Ventures LLC – This program is a joint venture between the Corporation and a major commercial insurer. The program invests in start-up and young technology companies in Connecticut by the use of seed or early stage financing.

Yankee Ingenuity Technology Program – This program was developed to encourage technological innovation through partnerships between Connecticut businesses and Connecticut colleges and universities.

BioScience Facilities Program – This program encourages the growth of Connecticut’s bioscience industry by providing financing to qualified biotechnology companies for the construction of laboratory and related space.

Connecticut BioSeed Program – This program was established to help accelerate the growth of early-stage biotech enterprises in Connecticut. The program typically invests up to \$500,000 in companies working to solve unmet medical needs.

Seed Investment Fund – This program addresses the needs of entrepreneurs as they endeavor to grow Connecticut-based emerging technology companies. The Seed Program provides funding to qualified non-bioscience companies in Connecticut. Seed investments of up to \$500,000 are structured as equity (preferred stock), convertible debt, or debt with warrants depending on the individual circumstances of the deals.

Pre-Seed Support Services – This program helps innovative, high technology entrepreneurs develop companies in Connecticut. The CI team provides mentoring, coordination of services and limited funding for business assistance to prepare the tech company for future investments.

Connecticut Clean Energy Fund – As required under Section 16-245n, during the audit period, CI administered this Fund. It was created under Public Act 98-28 as the Renewable Energy Investment Fund. The Fund is intended to promote the production and utilization of clean energy, and is commonly referred to as the Connecticut Clean Energy Fund (CCEF). Although the CCEF should be considered a CI program, its financial records and activities are kept separate from CI, as its purpose is distinctly different from that of CI. A separate independent audit is done for the CCEF.

In addition, in the footnotes to its financial statements for the fiscal year ended June 30, 2007, the following organizations are identified as blended component units of the Corporation, that, although legally separate entities, are in substance, part of the Corporation's operations:

Connecticut Technology Development Corporation (CTDC) – The CTDC is a CI wholly owned for-profit corporation, used to address the need by new biotech firms for wet laboratory space in “move-in” condition. The CTDC activities during the 2006-2007 fiscal year consisted mainly of rent, utilities, and depreciation expenses at 25 Science Park in New Haven. The total expenses of CTDC during the fiscal year ended June 30, 2007 were \$389,277. These amounts are included in the Corporation's financial statements.

Connecticut Innovations Educational Foundation (CIEF) – The CI Board approved the creation of the CIEF at its May 14, 2001 meeting. It is a non-stock corporation, exempt from federal income taxes under Internal Revenue Code Section 501(c)(3), in which CI is the sole member. At its March 22, 2004 meeting, the Board authorized several CI and CCEF programs to be run through the CIEF, including the Technology Scholar Program, the Yankee Ingenuity Technology Competition, the Clean Energy Freedom Bus, and the Connecticut Clean Energy Fund Yankee Ingenuity Technology Competition. CI explains that the Foundation was created so that it could solicit funds from external sources as a 501(c)(3) corporation, to provide additional funding for the programs. Apparently, the Foundation was not successful in its fund raising efforts, and the CI Board approved the dissolution of the Foundation at its July 28, 2006 meeting. CI assumed responsibility over the conduct and ongoing programs of the Foundation.

Organizationally, the Corporation is divided into five major areas:

- Finance and Administration - responsible for accounting, administration, finance, and information technology support.
- Investments – responsible for identifying opportunities that fall within the Corporation's scope and providing, where appropriate, capital for invention and innovation when financial aid is not available from normal commercial sources.
- External Relations – responsible for communications, marketing and media relations.
- Business Development – responsible for developing and supporting business opportunities for CI and its portfolio companies.
- Connecticut Clean Energy Fund Operations – responsible for the operation of the Connecticut Clean Energy Fund.

Significant State Legislation:

An Act Concerning the Renewable Energy Investment Fund – Public Act 07-152, Section 1, effective October 1, 2007, requires that the Renewable Energy Investment Fund shall no longer be managed by CI, but shall be within CI for administrative purposes only. It also establishes a Renewable Energy Investments Board of not more than fifteen individuals with knowledge and experience in matters related to the purpose and activities of the Renewable Energy Investment Fund. The Act requires the Board to act on matters related to the Renewable Energy Investment Fund, including, but not limited to, expenditure of funds and development of a comprehensive plan that must be submitted to the Department of Public Utility Control for approval. The Board shall issue annually a report to the Department of Public Utility Control describing the programs and activities of the Renewable Energy Investment Fund and shall provide a copy of such report, to the joint standing committees of the General Assembly having cognizance of matters relating to energy and commerce and the Office of Consumer Counsel.

An Act Authorizing and Adjusting Bonds of the State for Capital Improvements and for Transportation Infrastructure Improvements and Concerning the Connecticut State University Infrastructure Act – Public Act 07-7, Section 13 (n), effective November 2, 2007, authorizes the proceeds of the sale of bonds not exceeding \$12,000,000 to recapitalize the programs of CI. Up to \$1,500,000 shall be made available for capital expenses associated with the Biobus.

Board of Directors and Administrative Officials:

Pursuant to Section 32-35 of the General Statutes, a 15-member Board of Directors governs the Corporation. Eight members are appointed by the Governor and four are appointed by various legislative leaders. In addition, the Commissioner of the Department of Economic and Community Development, the Commissioner of the Department of Higher Education and the Secretary of the Office of Policy and Management serve as ex-officio members. Subsection (c) of Section 32-35 provides that the Chairperson of the Board shall be appointed by the Governor with the advice and consent of the Legislature.

As of June 30, 2007, the members of the Board of Directors were as follows:

Appointed by the Governor:

Elaine A. Pullen, Chairperson
Louis N. George, Esq.
R. Carol Muradian
John W. Olsen
Paul R. Pescatello, Esq.
Rafael A. Santiago
George W. Schiele
Chandler Howard

Legislative Appointments:

Thomas J. Clark
Alan K. Greene

Auditors of Public Accounts

Harris L. Marcus
E. Charles McClenachan, Ph.D.

Ex-Officio:

Valerie F. Lewis, Commissioner of Higher Education
Joan McDonald, Commissioner of Economic and Community Development
Robert Genuario, Secretary of the Office of Policy and Management

In addition to the above members, James F. Abromaitis, Commissioner of Economic and Community Development and John A. Mengacci, Undersecretary of the Office of Policy and Management also served as ex-officio members of the Board during the audit period.

Elaine Pullen served as Chairperson of the Board until her resignation effective July 31, 2007. Edward M. Bowman, Jr. served as Chairperson from August 10, 2007 until his resignation effective March 18, 2008. Joan McDonald was appointed Chairperson on May 27, 2008.

In addition, the Board has set up several Committees and Sub-committees to expedite certain business activities of the Corporation as well as to maintain controls over its transactions. The Corporation has the following four standing committees: Audit, Compliance and Governance Committee; Finance, Operations and Compensation Committee; Eli Whitney Investment Committee; and the Clean Energy Investment Committee. The Corporation also has several advisory committees that include: the Eli Whitney Advisory Committee, the Clean Energy Advisory Committee, the Clean Energy Investments Advisory Committee, the Valuation Committee, the Executive Advisory Committee, the BioSeed Advisory Committee, the Technology Review Committee, and the Projects Subcommittee of the Clean Energy Fund.

On April 28, 2006, the Board appointed Peter Longo to the position of Deputy Executive Director. Frank A. Dinucci served as President and Executive Director, effective October 2, 2006 until his resignation on April 30, 2007. John Mengacci served as Acting Executive Director effective April 13, 2007 until his resignation on April 27, 2007. On October 26, 2007 the Board appointed Peter Longo to the position of President and Executive Director.

RÉSUMÉ OF OPERATIONS:

The State of Connecticut provided significant initial financing for the Corporation's programs through the proceeds of General Obligation Bonds. It is these bond proceeds and any net income from operations that are used to finance the Corporation's investments.

Bond payments are processed through the State Comptroller's centralized payment system and are recorded on both the State and the Corporation books. The State Comptroller records State bond proceeds to finance loans and investments as expenditures, while the Corporation records them as investments and as contributed capital.

The Corporation also uses the centralized State payment system for processing payroll and other operating expenses. As provided for by subsection (b) of Section 32-41a of the General Statutes, all investment income and loan repayments are deposited into the Corporation's "operating account."

State Accounts:

As indicated above, State expenditures related to Connecticut Innovations, Incorporated include bond fund proceeds to finance various grants and investments. They also include certain operating expenses processed through the State's centralized processing systems. These transactions are processed through two State Funds - a special revenue fund and an enterprise fund (Connecticut Innovations Incorporated Fund). The special revenue fund is used to process certain grant awards authorized by the Legislature through various authorizing special acts and the action of the State Bond Commission. There were no Special Revenue Fund expenditures during the audit period.

The Connecticut Innovations Incorporated Fund is an enterprise fund authorized by Section 32-41a of the General Statutes. That Statute provides that this fund be used to carry out the purposes of CI, and also for the repayment of State bonds when required by the State Bond Commission. Total bond fund monies authorized by Sections 32-41, 32-41b, and 31-41o, amounted to \$114,801,000 as of June 30, 2007. Expenditures charged to the Fund during the audited period consisted entirely of payroll costs for CI and the CCEF, which were funded by cash transfers from CI to the Fund. A summary of Fund expenditures for the audited period follows:

	<u>Fiscal Year Ended</u>	
	<u>June 30, 2007</u>	<u>June 30, 2006</u>
	\$	\$
Personal Services	3,137,264	2,925,238
Fringe Benefits	<u>1,649,119</u>	<u>1,518,782</u>
Totals	<u>\$ 4,786,383</u>	<u>\$ 4,444,020</u>

The increase in Personal Services and fringe benefits is due to an increase in salaries, headcount and vacation accrual payouts at separation. There were no State expenditures made from the Enterprise Fund for investment purposes.

Connecticut Innovations, Incorporated Accounts:

As previously indicated, pursuant to subsection (b) of Section 32-41a of the General Statutes, all investment income, loan repayments, and grants with payback provisions are deposited into a Corporation account (i.e. "operating account"). The operating account is used to pay administrative expenses including the transfers to the enterprise fund for reimbursements of personal services, fringe benefits and other administrative costs charged to the fund.

Any excess funds in the operating account are transferred to short-term investments and marketable securities, including the State Treasurer's Short Term Investment Fund (STIF) to earn investment income. It should be noted that the Corporation may be required by the Bond Commission to repay the moneys advanced by the Bond Commission, including interest, under terms the Commission might find desirable and consistent with the purposes of the Corporation. As of June 30, 2007, the Bond Commission had not requested repayment of any principal or interest.

The financial position of the Corporation as of June 30, 2006 and 2007, per its audited financial statements, is presented below. It should be noted that certain 2005-2006 amounts have been reclassified to be consistent with the 2006-2007 presentation. The following amounts do not include

the Connecticut Clean Energy Fund.

	<u>As of June 30,</u>	
Assets	<u>2007</u>	<u>2006</u>
Current Assets:		
Cash and cash equivalents	\$ 24,793,944	\$ 29,270,633
Marketable securities	16,694,181	15,697,380
Current portion of investments	1,885,189	1,690,630
Due from the State of Connecticut	865	1,748
Other assets	<u>888,746</u>	<u>829,113</u>
Total current assets	<u>44,262,925</u>	<u>47,489,504</u>
Non-Current Assets		
Portfolio Investments:		
Eli Whitney investments	27,379,667	19,924,662
Investment in BioScience Facilities	12,739,819	14,782,223
Investment in CT Emerging Enterprises	1,269,596	1,502,735
Investment in Next Generation Ventures	228,890	928,697
Other investments	<u>752,672</u>	<u>333,015</u>
Total investments	42,370,644	37,471,332
Less current portion	<u>(1,885,189)</u>	<u>(1,690,630)</u>
Investments - non-current	40,485,455	35,780,702
Capital assets, net of depreciation	<u>1,140,155</u>	<u>1,252,963</u>
Total non-current assets	<u>41,625,610</u>	<u>37,033,665</u>
Total Assets	<u>\$ 85,888,535</u>	<u>\$ 84,523,169</u>
Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 707,526	\$ 605,449
Custodial liability	250,000	0
Due to related parties	<u>104,568</u>	<u>41,498</u>
Total liabilities	<u>1,062,094</u>	<u>646,947</u>
Net Assets		
Invested in capital assets	1,140,155	1,252,963
Unrestricted	<u>83,686,286</u>	<u>82,623,259</u>
Total net assets	<u>84,826,441</u>	<u>83,876,222</u>
Total Liabilities and Net Assets	<u>\$ 85,888,535</u>	<u>\$ 84,523,169</u>

The Corporation makes risk capital investments of no more than six million dollars, with the approval of the Finance Committee of the Board of Directors, in high technology applicant companies. Investments greater than six million dollars are possible, with approval of the full Board of Directors. The Corporation primarily makes investments in equity securities of emerging high-tech companies. It has substantially eliminated the use of royalty financing arrangements but continues to recover the cost and revenues of past royalty arrangements. The Corporation has approximately 70 percent of its investments in equity securities.

In the absence of readily determined market values, investments are carried at fair value as estimated by the valuation committee of the Corporation, using United States Private Equity Valuation Guidelines promulgated by the Private Equity Investment Guidelines Group. As is commonplace with investments such as those held by CI, and as disclosed in the CI's audited financial statements, due to the inherent uncertainty of valuation, those estimated values may differ significantly from the amounts ultimately realized from the investments, and the differences could be material.

CI also provides loans that are generally convertible into equity to Connecticut companies to bring new high technology products to market. Loans may be used for any business-related purpose such as hiring, marketing, research and development, inventory buildup and capital expenditures. A loan must be repaid within six years according to an arranged payment schedule.

A schedule of revenues, expenses and change in net assets for the fiscal years ended June 30, 2006 and 2007, follows. The information was obtained from the Corporation's audited financial statements, and does not include the Connecticut Clean Energy Fund.

	<u>Fiscal Year Ended June 30,</u>	
	<u>2007</u>	<u>2006</u>
Operating Revenues:		
Interest on short-term investments and cash deposits	\$ 2,117,204	\$ 1,442,315
Interest on investments	1,125,959	1,576,558
Other income	<u>193,010</u>	<u>423,316</u>
Total Revenue	<u>3,436,173</u>	<u>3,442,189</u>
Operating Expenses:		
Compensation and benefits	2,573,188	2,209,590
General and administrative expenses	1,616,917	2,133,308
Grants and programs	<u>197,881</u>	<u>374,825</u>
Total expenses	<u>4,387,986</u>	<u>4,717,723</u>
Operating Loss	<u>(951,813)</u>	<u>(1,275,534)</u>
Non-Operating Revenues (Expenses):		
Unrealized gain (loss) on investments	1,321,805	11,679,330
Realized gain (loss) on sale of investments	<u>580,227</u>	<u>(9,465,713)</u>
Total non-operating revenues (expenses)	<u>1,902,032</u>	<u>2,213,617</u>
Change in Net Assets	<u>\$ 950,219</u>	<u>\$ 938,083</u>

Total revenues decreased by \$6,016 in 2007. Interest on short term investments and cash deposits increased \$674,889 in 2007 due to higher average cash on hand and interest rate increases for the fiscal year. Interest on portfolio investments decreased by \$450,599 as a result of pay-offs and pay-downs of loans. Other income decreased by \$230,306 due to a decrease in the receipt of royalties.

Compensation and benefits increased by \$363,958 primarily as a result of increases in salaries, headcount and the payment of vacation accruals at separation.

General and administrative expenses decreased by \$516,391 during the 2006-2007 fiscal year due primarily to decreases in consulting fees and office related expenses.

Total expenditures for grants and scholarship programs in 2007 were \$197,881, a decrease of \$176,944 over last year. The decrease was largely due to a decline in funding of the Yankee Ingenuity Technology Program in 2007.

Net realized gains on investments for the year were \$580,227 as compared to realized losses of \$9.5 million in 2006. In 2007, the realized gains were from the sale of public securities and recoveries of investments written off in prior years. The \$9.5 million in realized losses in 2006 resulted from write-offs totaling \$14.3 million of investments in several portfolio companies partially offset by \$4.8 million in realized gains primarily from the sale of public securities.

The CI Board approved \$6,453,600 for new investments during the fiscal year ended June 30, 2007, and funded \$6,512,477. The Eli Whitney Fund comprised the majority of the approved and funded amounts. In addition, CI provided funding of \$374,826 for grants and scholarships during the audited period.

Connecticut Clean Energy Fund:

The Renewable Energy Investment Fund (commonly referred to as the Connecticut Clean Energy Fund) was established in July 1998 under Title 16, Section 16-245n of the General Statutes. Prior to October 1, 2007, said Section required that Connecticut Innovations administer the Connecticut Clean Energy Fund.

Section 16-245n provides that on or after January 1, 2000, the Department of Public Utility Control shall assess or cause to be assessed a charge per kilowatt-hour to each end-user of electrical service in the State. It is this assessment that provides the financing for the Fund. Unlike the majority of Connecticut Innovations' investments, the Connecticut Clean Energy Fund is not limited to Connecticut businesses. CI is authorized to use any amount in the Fund for expenditures that promote investment in renewable energy sources in accordance with a comprehensive plan developed by it to foster the growth, development and commercialization of renewable energy sources and related enterprises and stimulate demand for renewable energy and deployment of renewable energy sources which serve end use customers in this state. Such expenditures may include, but not be limited to, grants, direct or equity investments, contracts or other actions which support research, development, manufacture, commercialization, deployment and installation of renewable energy technologies, and actions which expand the expertise of individuals, businesses and lending institutions with regard to renewable energy technologies.

The Fund's two key strategic thrusts are the support of renewable energy technologies (fuel cell, wind, solar, biomass conversion, tidal energy, ocean thermal, etc.) and infrastructure and market support (education and outreach, tradable renewable certificates, entrepreneurial stimulation, etc.).

Prior to October 1, 2007, Section 16-245n, subsection (d), established a Renewable Energy Investments Advisory Committee to assist CI in matters related to the Connecticut Clean Energy Fund. The committee shall consist of not more than 12 individuals with knowledge and experience in matters related to the purpose and activities of the Fund. Three of the members are appointed by the Connecticut Innovations' Board of Directors. Of the remaining nine members, two shall be State officials appointed by the Governor, one shall be a Gubernatorial appointee with experience

regarding renewable energy resources and one member each is appointed by the Speaker of the House of Representatives, the President Pro-Tempore of the Senate, the majority leaders of the House of Representatives and the Senate, and the minority leaders of the House of Representatives and the Senate. This Advisory Committee is known as the Clean Energy Advisory Committee of the Connecticut Clean Energy Fund. There is also a Clean Energy Investment Committee of the CI Board of Directors currently made up of six CI Board members. Before any investment or grant proposal, etc., is funded, it must be approved by the Clean Energy Investment Committee, which generally acts on the recommendations made by the Advisory Committee.

The members of the Connecticut Clean Energy Fund Advisory Committee as of June 30, 2007, were as follows:

Timothy Bowles, Chairman
Marian Chertow
Donald W. Downes
Norma J. Glover
Richard C. Lichter
Robert Maddox
John Mengacci
William T. Sellay
Margery C. Winters

Appointed by the Board of Directors of Connecticut Innovations Inc.:

Jerome P. Peters, Jr.
John W. Olsen
E. Charles McClenachan, Ph.D.

Timothy Bowles was appointed Chairman on October 25, 2004.

Subsequent to the audit period, pursuant to Public Act 07-152, the CCEF Advisory Committee was replaced by the Connecticut Clean Energy Fund Board effective October 1, 2007. The CCEF Board has up to 15 members, consisting of the Consumer Counsel and the head or designee of the Office of Policy and Management, and the Department of Environmental Protection. The remaining eleven board members are appointed by the governor, the legislative leadership and CI's Board of Directors. The following members have been appointed through February 2008:

Timothy Bowles, Chairman
Mary Healey, Consumer Counsel
John Mengacci (designee of the Office of Policy and Management)
Scott DeVico (designee of the Department of Emergency Management and Homeland Security)
Tracy Babbidge (designee of the Department of Environmental Protection)
Robert Maddox
Norma Glover
Patricia Wrice
Carol Muradian

Auditors of Public Accounts

Appointed by the Board of Directors of Connecticut Innovations Inc.

John Olsen

Jerry Peters

Edward M. Bowman, Jr.

3 vacancies

The financial position of the Connecticut Clean Energy Fund as of June 30, 2006 and 2007, as presented in its audited financial statements, follows. It should be noted that certain 2005-2006 amounts have been reclassified to be consistent with the 2006-2007 presentation.

	<u>As of June 30,</u>	
	<u>2007</u>	<u>2006</u>
Assets	\$	\$
Cash and cash equivalents	48,791,662	38,211,160
Marketable securities	33,055,835	31,578,619
Utility Customer Assessments Receivable	2,073,650	1,910,000
Due from related parties	104,568	22,750
Investments	427,421	1,168,903
Other assets	80,517	4,969
Restricted assets	<u>830,415</u>	<u>879,325</u>
Total Assets	<u>\$ 85,364,068</u>	<u>\$ 73,775,726</u>
Liabilities and Net Assets		
Liabilities:	\$	\$
Accrued Expenses	<u>783,887</u>	<u>1,072,232</u>
Total Liabilities	<u>783,887</u>	<u>1,072,232</u>
Net Assets:		
Restricted	830,415	879,325
Unrestricted	<u>83,749,766</u>	<u>71,824,169</u>
Total Net Assets	<u>84,580,181</u>	<u>72,703,494</u>
Total Liabilities and Net Assets	<u>\$ 85,364,068</u>	<u>\$ 73,775,726</u>

Connecticut Clean Energy Fund revenue, expenses and the change in net assets for the fiscal years ending June 30, 2006 and 2007, are presented below. The information was taken from the Connecticut Clean Energy Fund audited financial statements for those fiscal years.

	<u>Fiscal Year Ended June 30,</u>	
	<u>2007</u>	<u>2006</u>
Revenues:	\$	\$
Utility Customer Assessments	22,841,350	21,538,969
Interest on short-term investments	3,834,314	2,462,457
Other income	<u>323,529</u>	<u>211,786</u>
Total Revenues	<u>26,999,193</u>	<u>24,213,212</u>

Expenditures/Expenses:

Program:

Grants	10,822,746	10,216,053
Program expenses	<u>2,109,107</u>	<u>1,533,547</u>
Total program expenses	12,931,853	11,749,600
General and administrative expenses	<u>1,650,627</u>	<u>1,732,310</u>
Total Expenditures and Expenses	14,582,480	13,481,910

Change in Net Assets Before Changes in the Fair Value of Investments	12,416,713	10,731,302
Net realized gain (loss) on investments	20,408	(3,019,450)
Net increase (decrease) in the fair value of investments	<u>(560,434)</u>	<u>7,302,121</u>
Net Change in Net Assets	11,876,687	15,013,973
Net assets, beginning of year	<u>72,703,494</u>	<u>57,689,521</u>
Net assets, end of year	<u>\$ 84,580,181</u>	<u>\$ 72,703,494</u>

Revenues from utility customer assessments increased by \$1,302,381 during the 2006-2007 fiscal year due to an increase in utility usage. Beginning in the 2005-2006 fiscal year, there was a statutory transfer of funds for debt service on the State of Connecticut Special Obligation Rate Reduction Bonds (2004 Series A) which were issued on June 23, 2004, in accordance with Public Act 03-6, Section 50, of the June 30, 2003, Special Session, effective August 20, 2003. The proceeds of these bonds were to be used in lieu of direct transfers from the CCEF to the General Fund. One-third of the one mill statutory ratepayer assessment will be used to cover the debt service portion on the bonds, resulting in a reduction in the Connecticut Clean Energy Fund revenues of an estimated \$8,600,000 per year.

Interest on short-term investments and cash deposits increased by \$1,371,857 in the 2006-2007 fiscal year due to an increase in the average cash balance on hand and higher interest rates.

Total expenditures for grants and programs in 2006-2007 were \$12,931,853. During 2006-2007, the Fund committed a total of \$27.4 million for new grants and programs.

In the 2007 fiscal year, the fair value of the Fund's investments decreased by \$741,482. There was a decrease in valuations with respect to equities of emerging renewable energy companies in which the Fund invests. Most of the Fund's investments were made in the early stages of the Fund's existence. As the Fund has evolved, it was determined that grant programs would provide more immediate results, and accordingly, CI shifted the Fund's focus from making investments to providing grants. Most of the recipients of the Fund's monies are selected based on detailed reviews of information submitted in response to the Fund's Requests for Proposals, which vary depending upon the particular program within the Fund. Investments still remain an option for the Fund.

During the 2006-2007 fiscal year the Board approved \$27,370,899 for new grants and programs. As of June 30, 2007, the Fund had outstanding commitments totaling \$24,953,164 that are expected to be funded over the next two fiscal years.

Other Examinations:

Auditors of Public Accounts

Independent public accountants audited the Corporation's financial statements and those of the Connecticut Clean Energy Fund for the year under review. Those audits attested that the financial statements presented fairly, in all material respects, the financial position of Connecticut Innovations, Incorporated and the Connecticut Clean Energy Fund for the year under review, and the results of its operations for those years in conformity with generally accepted accounting principles.

The independent public accountants' reports included an explanatory paragraph regarding the Corporation's use of estimates to determine the fair value of a significant portion of its assets in the absence of readily ascertainable market values. Essentially, it was concluded that the procedures the Corporation used to arrive at the estimated values of its investments were reasonable and appropriately documented; however, because of the inherent uncertainty of valuation, those estimated values may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material.

As an integral part of their financial statement audits, the independent public accountants also provided reports on compliance and on internal control over financial reporting. These reports disclosed no instances of noncompliance concerning these requirements. The reports on internal control indicated that no material weaknesses in internal control were identified.

CONDITION OF RECORDS

Our review of the records of the Connecticut Innovations, Incorporated revealed the following areas that warrant comment.

Connecticut Clean Energy Fund Revenues:

Criteria: A system of internal control over revenues should include procedures requiring that revenues be supported by documentation substantiating the accuracy and completeness of the amounts due compared to those that are collected.

Condition: The Connecticut Clean Energy Fund receives monthly payments from two utility companies, representing charges assessed to end-users of electric services as mandated under Section 16-245n of the General Statutes, that aggregated over \$22,622,000 during the audit period.

During the prior audit we reported that documentation supporting the amounts paid by the companies was insufficient to determine whether all of the required assessments were collected. Although CI has continued discussions with the utility companies and the Department of Public Utility Control to resolve this insufficiency, CI has been unable to develop a process to verify the accuracy and completeness of the supporting reports.

Effect: There is reduced assurance that the Connecticut Clean Energy Fund received all of the revenue to which it was entitled.

Cause: CI has been unable to develop a process to adequately confirm that all collected revenues due have been collected.

Recommendation: CI should institute procedures to ensure that the revenue collected for the Connecticut Clean Energy Fund represents all of the monies that the Connecticut Clean Energy Fund is due. Also, consideration should be given to reviewing prior years' payments to ensure that the Connecticut Clean Energy Fund received all of the revenue that it was statutorily required to receive. (See Recommendation 1.)

Agency Response: "CI has met with the Department of Public Utility Control (DPUC) and the Office of Consumer Counsel (OCC) to discuss an approach to auditing the documentation provided by the utility companies in support of ratepayer assessments deposited with the Connecticut Clean Energy Fund. Since CI lacks the statutory authority to audit the utilities financial records, the OCC has agreed to assist us in this matter by auditing the supporting documentation for accuracy and completeness. The OCC is contacting the utilities to begin the process."

Conflicting Statutory Reporting Provisions:

Criteria: Section 32-47a of the General Statutes requires CI to submit a business plan containing a summary of its projected operations for the year and to prepare an annual report which shall include the following information with respect to new and outstanding financial assistance provided by CI during the twelve-month period ending on June thirtieth for each financial assistance program administered by the corporation: (1) a list of the names, addresses and locations of all recipients of such assistance; (2) for each such recipient: (A) the business activities, (B) the Standard Industrial Classification Manual codes, (C) the gross revenues during the recipient's most recent fiscal year, (D) the number of employees at the time of application, (E) whether the recipient is a minority or woman-owned business, (F) a summary of the terms and conditions for the assistance, including the type and amount of state financial assistance, job creation or retention requirements, and anticipated wage rates, and (G) the amount of investments from private and other nonstate sources that have been leveraged by the assistance; (3) the economic benefit criteria used in determining which applications have been approved or disapproved; and (4) for each recipient of assistance on or after July 1, 1991, a comparison between the number of jobs to be created, the number of jobs to be retained and the average wage rates for each such category of jobs, as projected in the recipient's application, versus the actual number of jobs created, the actual number of jobs retained and the average wage rates for each such category. The report shall also indicate the actual number of full-time jobs and the actual number of part-time jobs in each such category and the benefit levels for each such subcategory. The report shall also include a summary of the activities of the corporation, including all activities to assist small businesses and minority business enterprises, as defined in Section 4a-60g, a complete operating and financial statement and recommendations for legislation to promote the purposes of the corporation. The corporation shall furnish such additional information upon the written request of any such committee at such times as the committee may request.

Section 32-40, subsection (c), of the General Statutes provides that all financial information obtained by CI concerning any applicant or project shall not be regarded as public records.

Condition: Our review of CI's Business Plan for the fiscal year ended June 30, 2007, revealed that CI incorrectly carried forward the budget for the fiscal year ended June 2006, resulting in a variance of net income reported of \$1,915,000.

Our review of CI's annual financial assistance report for the fiscal year ended June 30, 2007, revealed that CI did not clearly report revenue, wage rate and benefit level data separately for each recipient of assistance; the data was reported in such a format that the identity of the individual recipients of assistance could not be linked with the data reported. In addition, the wage

rate data was not reported for jobs to be created and retained.

Effect: The Corporation did not disclose all of the information required under Section 32-47a of the General Statutes.

Cause: It appears that the wrong budget was reported in the Business Plan due to human error.

CI reported the data in an encrypted format because it has taken the position that such information is confidential in accordance with Section 32-40, subsection (c). Although the information was collected, we could not determine why CI did not report the wage rate data for jobs to be created and retained.

Recommendation: CI should strengthen internal controls to ensure the correct budget is reported in the Business Plan. CI should also seek legislative clarification to resolve the apparent statutory conflict between Section 32-47a and 32-40, subsection (c), to ensure that all information is reported consistent with the legislative intent. (See Recommendation 2.)

Agency Response: “CI will strengthen its internal control over the aggregation of financial data contained in its annual business plan submission by requiring the Vice President of Finance & Administration to review and approve all financial data contained in the business plan prior to submission.

During the 2007 legislative session, the Commerce Committee raised a bill that would have reconciled the two different provisions of CI’s statutes referenced above. The bill died on the last day of the legislative session. However, in an effort to comply with the legislature’s intent, CI filed its FY07 report consistent with the provisions of the bill. During this current legislative session, the Commerce Committee has raised S.B. 547 An Act Concerning Connecticut Innovations, Inc on CI’s behalf. The bill seeks to amend the requirements of C.G.S. 32-47a to allow CI to be in compliance with the requirements of C.G.S. 32-40(a).”

Investments:

Criteria: Section 32-35(d) of the General Statutes requires that the board of directors of the Corporation shall adopt written procedures for awarding loans, grants and other financial assistance, including eligibility criteria, the application process and the role played by the Corporation’s staff and board of directors.

Section 32-40 of the General Statutes requires that all applications for financial aid shall be processed in accordance with the written procedures adopted by the Corporation under subdivision (5) of subsection (d) of Section 32-35. The finance committee of the corporation shall approve or deny each application recommended by the executive director. If the finance committee

approves an application, such committee may authorize the Corporation to enter into an agreement or agreements on behalf of the Corporation to provide financial aid to the applicant.

Condition: Our review disclosed that CI funded one seed investment in the amount of \$450,000 without obtaining approval from the finance committee. This was the only seed investment funded during the audit period. We did note that the investment was approved by a majority of the investment managers, the chief investment officer and the president and executive director in accordance with CI's operating procedures.

Effect: There is non-compliance with the General Statutes.

Cause: There is a conflict between CI's operating procedures and Section 32-40 of the General Statutes. CI's operating procedures state that approval by the Board, or a duly authorized committee thereof, is not required for seed investments up to \$500,000.

Recommendation: CI should amend its operating procedures to ensure compliance with Section 32-40 of the General Statutes. (See Recommendation 3.)

Agency Response: "CI agrees that its operating procedures are not in compliance with the General Statutes. At its January 29, 2007 meeting, the CI Board of Directors passed a resolution allowing the CI investment team to approve seed investments of up to \$500,000. Upon passage of the board resolution, CI drafted an amendment to its operating procedures and presented it to the board's Audit, Compliance & Governance Committee for approval. Following the committee's approval, CI posted public notice of the amendment to the operating procedures in the Connecticut Law Journal for 30 days and then brought the amendment to the CI Board of Directors for approval. The Board voted to approve the amendment to the operating procedures and allocated \$2,000,000 to the program.

On CI's behalf the Commerce Committee has raised S.B. 547 An Act Concerning Connecticut Innovations, Inc which seeks to amend Section 32-40 of the General Statutes to reflect CI's operating procedures for seed investments."

Auditors' Concluding Comment:

Until legislation is passed amending Section 32-40 of the General Statutes, CI should amend its operating procedures to ensure compliance with the General Statutes.

Personnel Policies – Time and Attendance:

Criteria:

In accordance with Sections 1-121 and 32-35(d) of the General Statutes, CI has established written procedures for most personnel matters. CI's Employee Handbook establishes that introductory employees are not eligible to take vacation or personal leave until they have successfully completed six months of employment. Any significant absence will automatically extend the introductory period by the length of the absence. Vacation days are accrued on a monthly basis and employees begin to accrue vacation days the first full month after their date of hire. In order to be eligible for severance payments, an employee must be employed for two years as of the date of separation. Sound business practices require that time and attendance information be recorded accurately and that employees be compensated only for time worked and/or earned.

Condition:

Our review of the time and attendance records of thirteen employees that were newly hired during the audit period disclosed that three employees were permitted to use vacation and/or personal leave prior to completing the six-month introductory period and one employee was also compensated for time not worked as follows:

- In the first instance, the employee used sixteen hours of vacation in two instances of eight hours.
- In the second instance, the employee used eight hours of personal leave and forty-eight hours of vacation leave, of which twenty-four hours had not yet accrued.
- In the third instance, the employee used seventy-two hours of leave time, of which twenty-two hours had not yet accrued. Although the employee was only two weeks short of completing the six-month introductory period, the leave time was taken after the employee had submitted a letter of resignation. Our review also disclosed that there is the appearance that the employee was compensated for, but did not work for the remaining twenty-two of twenty-five days subsequent to the employee's resignation announcement. Although there were signed timesheets on hand, our review of records documenting the employee's access to the building, the removal of the employee's authority by the Board of Directors, the appointment of a temporary replacement, and inquiries of CI personnel suggest that the employee was compensated for time not worked.

Our review also disclosed that in the above instances, leave time was not entered into the time and attendance records on the dates it was used, but was entered as being used on dates subsequent to the employees meeting the six-month introductory period. Our review disclosed that secondary unsigned timesheets were attached to the original signed timesheets to track the differences between time actually charged and the time entered into the time and attendance system.

Effect: There is non-compliance with CI's Employee Handbook. The time and attendance records were not maintained in an accurate manner increasing the risk that additional time and attendance errors could occur. When employees are permitted to use leave time that they have not yet earned, there is the risk that these amounts will not be recovered if the employee does not successfully complete the employee's six-month introductory period or resigns.

For the employee noted above who resigned, it appears that the employee was compensated for a total of \$25,295 for regular and leave time pay and fringe benefits to which the employee was not entitled.

Cause: It appears that CI's practice is to grant vacation and personal leave in advance of completing the six-month introductory period provided supervisory approval is obtained. We were informed that leave time was not entered into the time and attendance system as used because CI personnel believed the Core-CT system would not permit the processing of leave time that had not yet accrued. We were informed that payments to the employee who resigned were made upon the direction of the Board of Directors.

Recommendation: CI should strengthen its internal controls to ensure compliance with CI's Employee Handbook and to ensure that employee time and attendance records are maintained in an accurate manner and employees are compensated only for time worked or earned. (See Recommendation 4.)

Agency Response: "As stated in our Employee Handbook, "CI reserves the right to make exceptions or vary from any of the rules, benefits, or policies contained in this handbook in its managerial discretion." As mentioned above, some introductory employees were granted advance vacation and personal leave time after supervisory (managerial) approval was obtained.

The arrangements in the third instance referenced above were implemented in connection with the resignation of the Executive Director and the transfer of his responsibilities to the Deputy Director as expressly provided for in Section 3.6 of CI's Bylaws, which were previously adopted by the Board of Directors pursuant to Section 32-11a(c) of the General Statutes. The Executive Director is appointed and serves at the pleasure of the Board of Directors pursuant to Section 32-38 of the General Statutes, and the transition arrangements referred to in the third instance were within the express statutory authority of the Board of Directors to exercise all powers of the corporation, which extend to all personnel matters, including compensation and benefits. It was the considered judgment of the Board of Directors, in the circumstances presented by the Executive Directors' resignation, that the transition arrangements that were implemented in this case were necessary to assure a smooth transition to a new Executive Director and were in the best

interests of the corporation. These arrangements included the immediate transfer of the responsibilities of the Executive Director to the Deputy Director, and, pending the effective date of the Executive Directors' resignation, the continuing availability of the Executive Director to assist the Deputy Director with transition matters on an "as needed" basis. That assistance did not require the Executive Director's presence in CI's offices at all times, which the Board of Directors believed might otherwise have been disruptive of transition efforts. To the extent that these transition arrangements may have involved exceptions to provisions of the Employee Handbook, they represented the permitted exercise of managerial discretion by the Board of Directors."

Auditors' Concluding Comment:

Section 32-35(d) of the General Statutes requires that the Board adopt written procedures for hiring, dismissing, promoting and compensating employees of the Corporation. Such employees of the Corporation include the position of the Executive Director. There was no written evidence that an "as needed" arrangement existed and no documentation to support that any work was performed by the employee during the 22 of 25 days cited above.

Regarding the instances of leave time used in advance, these instances do not appear to be isolated or unusual instances, but rather reflect the current practice of CI, which is contrary to the policy included in the Employee Handbook. In addition, CI did not require written agreements governing the repayment of advanced leave time used should the employees resign prior to earning the time used, as was the case in the third instance cited in the condition above. In this instance, CI made no attempts to collect the vacation leave paid that was never earned.

Personnel Policies - Telecommuting:

Criteria: In accordance with Sections 1-121 and 32-35(d) of the General Statutes, CI has established written procedures for most personnel matters. CI's Operating Procedures require that the Board shall establish personnel policies including policies with respect to telecommuting. Sound business practices require that formal telecommuting policies and agreements be in place before the telecommuting period begins.

Condition: Our review disclosed that although CI has no telecommuting policies or agreements in place, employees are permitted to telecommute. We noted that one employee in the Clean Energy Fund telecommutes on a weekly basis and exempt employees are permitted to telecommute on an intermittent basis based on individual circumstances. We were informed that telecommuting privileges are typically granted when employees must attend meetings close to home, during weather emergencies or for the duration of a particular

project.

Effect: Telecommuting could occur that might not be in the best interests of CI. Without formal policies in place, employees cannot be properly monitored and there could be conflicts regarding workers' compensation coverage, the protection of confidential data, and other aspects of the work relationship.

Cause: It appears that CI's practice is to grant exempt employees telecommuting privileges without having an established telecommuting policy in place.

Recommendation: CI should institute written policies and procedures related to telecommuting that include formal telecommuting agreements. (See Recommendation 5.)

Agency Response: "The employee discussed above received verbal permission from CI management to telecommute. CI has amended its Employee Handbook to include written policies and procedures related to telecommuting that include formal telecommuting agreements."

RECOMMENDATIONS

Status of Prior Audit Recommendations:

- CI should institute procedures to ensure that the revenue collected for the Connecticut Clean Energy Fund represents all of the monies that the Connecticut Clean Energy Fund is due. Also, consideration should be given to reviewing prior years' payments to ensure that the Connecticut Clean Energy Fund received all of the revenue that it was statutorily required to receive. This recommendation is repeated. (See Recommendation 1.)
- CI should seek legislative clarification to resolve the apparent statutory conflict between Section 32-47a and 32-40, subsection (c), to ensure that all information is reported consistent with the legislative intent. This recommendation is repeated to reflect current conditions. (See Recommendation 2.)

Current Audit Recommendations:

- 1. CI should institute procedures to ensure that the revenue collected for the Connecticut Clean Energy Fund represents all of the monies that the Connecticut Clean Energy Fund is due. Also, consideration should be given to reviewing prior years' payments to ensure that the Connecticut Clean Energy Fund received all of the revenue that it was statutorily required to receive.**

Comment:

The Connecticut Clean Energy Fund receives monthly payments from two utility companies, representing charges assessed to end-users of electric services as mandated under Section 16-245n of the General Statutes, that aggregated over \$22,622,000 during the audit period. During the prior audit we reported that documentation supporting the amounts paid by the companies was insufficient to determine whether all of the required assessments were collected. Although CI has continued discussions with the utility companies and the Department of Public Utility Control to resolve this insufficiency, CI has been unable to develop a process to verify the accuracy and completeness of the supporting reports.

- 2. CI should strengthen internal controls to ensure the correct budget is reported in the Business Plan. CI should also seek legislative clarification to resolve the apparent statutory conflict between Section 32-47a and 32-40, subsection (c), to ensure that all information is reported consistent with the legislative intent.**

Comment:

Our review of CI's Business Plan for the fiscal year ended June 30, 2007, revealed that CI incorrectly carried forward the budget for the fiscal year ended June 30, 2006, resulting in a variance of net income reported of \$1,915,000. Our review of CI's annual financial assistance report for the fiscal year ended June 30, 2007, revealed that CI did not clearly report revenue, wage rate and benefit level data separately for each recipient of assistance; the data was reported

in such a format that the identity of the individual recipients of assistance could not be linked with the data reported. In addition, the wage rate data was not reported for jobs to be created and retained.

3. CI should amend its operating procedures to ensure compliance with Section 32-40 of the General Statutes.

Comment:

Our review disclosed that CI funded one seed investment in the amount of \$450,000 without obtaining approval from the finance committee.

4. CI should strengthen its internal controls to ensure compliance with CI's Employee Handbook and to ensure that employee time and attendance records are maintained in an accurate manner and employees are compensated only for time worked or earned.

Comment:

Our review of the time and attendance records of thirteen employees that were newly hired during the audit period disclosed that three employees were permitted to use vacation and/or personal leave prior to completing the six-month introductory period and one employee was also compensated for time not worked.

5. CI should institute written policies and procedures related to telecommuting that include formal telecommuting agreements.

Comment:

Our review disclosed that although CI has no telecommuting policies or agreements in place, employees are permitted to telecommute. We noted that one employee in the Clean Energy Fund telecommutes on a weekly basis and exempt employees are permitted to telecommute on an intermittent basis based on individual circumstances. We were informed that telecommuting privileges are typically granted when employees must attend meetings close to home, during weather emergencies or for the duration of a particular project.

INDEPENDENT AUDITORS' CERTIFICATION

As required by Section 2-90 and Section 1-122 of the General Statutes, we have conducted an audit of Connecticut Innovations, Incorporated's activities for the fiscal year ended June 30, 2007. This audit was primarily limited to performing tests of the Corporation's compliance with certain provisions of laws, regulations, contracts and grant agreements, including but not limited to a determination of whether the Corporation 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 Corporation's internal control policies and procedures for ensuring that the provisions of certain laws, regulations, contracts and grant agreements applicable to the Corporation are complied with. The financial statement audit of Connecticut Innovations, Inc., for the fiscal year indicated above, was conducted by the Corporation'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 Connecticut Innovations, Inc. 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 Financial Operations and Compliance:

In planning and performing our audit, we considered the Corporation's internal control over its financial operations and its compliance with requirements as a basis for designing our auditing procedures for the purpose of evaluating the Corporation's financial operations and compliance with certain provisions of laws, regulations, contracts and grant agreements, but not for the purpose of providing assurance on the effectiveness of the Corporation's internal control over those control objectives. Our consideration of internal control included, but was not limited to, the following areas:

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

A *control deficiency* 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 on a timely basis unauthorized, illegal, or irregular transactions. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Corporation's ability to properly initiate, authorize, record, process, or report financial data reliably consistent with management's direction, and/or comply with certain provisions of laws, regulations, contracts, and grant agreements such that there is more than a remote likelihood that noncompliance with laws, regulations, contracts and grant agreements that is more than inconsequential will not be prevented

or detected by the Corporation's internal control.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that noncompliance which could result in significant unauthorized, illegal, irregular or unsafe transactions and/or material noncompliance with certain provisions of laws, regulations, contracts, and grant agreements that would be material in relation to the Corporation's financial operations will not be prevented or detected by the Corporation's internal control.

Our consideration of the internal control over the Authority's financial operations, and compliance with requirements would not necessarily identify all deficiencies in the internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over the Authority's financial operations and compliance with requirements that we consider to be material weaknesses, as defined above.

Compliance and Other Matters:

As part of obtaining reasonable assurance about whether the Corporation 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 Corporation's financial operations for the fiscal year ended June 30, 2007, 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 Corporation'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 the Corporation's management in the accompanying "Condition of Records" and "Recommendations" sections of this report.

The Corporation's response to the findings identified in our audit is described in the accompanying "Condition of Records" sections of this report. We did not audit the Corporation's response and, accordingly, we express no opinion on it.

This report is intended for the information of the Governor, the State Comptroller, the Appropriations Committee of the General Assembly and the Legislative Committee on Program

Review and Investigations. However, this report is a matter of public record and its distribution is not limited. Users of this report should be aware that our audit does not provide a legal determination of the Corporation'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 Innovations, Incorporated during our examination.

Lisa G. Daly
Principal Auditor

Approved:

Kevin P. Johnston
Auditor of Public Accounts

Robert G. Jaekle
Auditor of Public Accounts