

# STATE OF CONNECTICUT



*AUDITORS' REPORT  
DEPARTMENT OF ECONOMIC AND COMMUNITY  
DEVELOPMENT  
FOR THE FISCAL YEARS ENDED JUNE 30, 2013 AND 2014*

**AUDITORS OF PUBLIC ACCOUNTS**  
JOHN C. GERAGOSIAN

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# STATE OF CONNECTICUT



## AUDITORS OF PUBLIC ACCOUNTS

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Hartford, Connecticut 06106-1559

JOHN C. GERAGOSIAN

February 16, 2017

### **AUDITORS' REPORT DEPARTMENT OF ECONOMIC AND COMMUNITY DEVELOPMENT FOR THE FISCAL YEARS ENDED JUNE 30, 2013 and 2014**

We have audited certain operations of the Department of Economic and Community Development in fulfillment of our duties under Section 2-90 of the Connecticut General Statutes. The scope of our audit included, but was not necessarily limited to, the years ended June 30, 2013 and 2014. The objectives of our audit were to:

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

Our methodology included reviewing written policies and procedures, financial records, minutes of meetings, and other pertinent documents; interviewing various personnel of the department, as well as certain external parties; and testing selected transactions. We obtained an understanding of internal controls that we deemed significant within the context of the audit objectives and assessed whether such controls have been properly designed and placed in operation. We tested certain of those controls to obtain evidence regarding the effectiveness of their design and operation. We also obtained an understanding of legal provisions that are significant within the context of the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contracts, grant agreements, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting instances of noncompliance significant to those provisions.

We conducted our audit in accordance with the standards applicable to performance audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides such a basis.

The accompanying *Résumé of Operations* is presented for informational purposes. This information was obtained from the department's management and was not subjected to the procedures applied in our audit of the department. For the areas audited, we identified:

1. Deficiencies in internal controls;
2. Apparent noncompliance with legal provisions; and
3. Need for improvement in management practices and procedures that we deemed to be reportable.

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

## COMMENTS

### FOREWORD

The Department of Economic and Community Development (DECD) operates principally under the provisions of Title 32, Chapter 578 and Title 10, Chapter 184b of the General Statutes. DECD administers programs and policies to promote business, community development, brownfield redevelopment, arts, culture and tourism, and is the state agency responsible for promoting economic growth. DECD also administered programs and matters related to housing under the provisions of Title 8, Chapter 127c of the General Statutes, until the programs were transferred from DECD pursuant to Public Act 13-234 effective July 1, 2013.

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

- Supports existing businesses and attracts new businesses and jobs with a wide range of programs and services to help companies prosper;
- Promotes Connecticut industries and businesses here at home, throughout the country, and across the globe;
- Strengthens Connecticut communities by providing funding and technical support for local community and economic development projects;
- Works to make tourism a leading economic contributor and a source of pride for Connecticut;

- Develops and strengthens the arts in Connecticut, making artistic experiences widely available to residents and visitors; and
- Helps to eliminate brownfield properties by promoting smart growth principles, strengthening public-private partnerships, and providing a one-stop resource for expertise.

Catherine H. Smith was appointed commissioner of DECD in April 2011 and served in that capacity throughout the audited period.

### **Significant Legislation**

Notable legislative changes that took effect during the audited period are presented below:

- **Public Act 12-1**, of the June 12, 2012 Special Session, effective upon passage:

Section 99 eliminated the requirement that the Connecticut Humanities Council operate in conjunction with DECD for strategic planning and financial reporting purposes with respect to culture, history, the arts, tourism, and the digital media and motion picture industries in Connecticut.

Section 112 established a Department of Housing (DOH) and made it, instead of DECD, the lead agency responsible for all housing matters. The act placed DOH in DECD for administrative purposes only and made it the successor to DECD with respect to housing-related functions, powers, and duties, including community development, redevelopment, and urban renewal.

Sections 199 to 201 expanded and made several programmatic changes to the Small Business Express Program (EXP), which consists of separate revolving loan, job incentive loan, and matching grant components. The act extended assistance to businesses based in other states if they have been registered to do business here or in other states for at least 12 months and have operations in Connecticut, and also extended assistance to more small businesses by raising the employee threshold from 50 to 100. The act extended the time period, (from within five years to five years or the loan's term, whichever is longer) during which a business receiving assistance under any component is subject to the statutory penalty for relocating out of state after receiving assistance, extended the maximum period for repaying a revolving loan from five to ten years, increased the maximum job incentive loan from \$250,000 to \$300,000, and allowed DECD to charge up to four percent interest on the loans. The act made several administrative changes, including allowing DECD to run the program by partnering with lenders participating in the Connecticut Credit Consortium, a DECD-administered small business assistance revolving fund. The act established a separate, nonlapsing General Fund account that must contain any funds the law requires to be deposited there, principal and interest loan repayments, and any other funds DECD receives for EXP.

Section 209 made a programmatic change to the First Five Plus Program, which provides loans, tax incentives, and other forms of economic development assistance to businesses that create jobs and invest capital within existing law's timeframes. It also allowed DECD to give a preference for First Five assistance to proposed business projects that will relocate overseas jobs to Connecticut. By law, a business receiving First Five assistance must commit to create at least 200 jobs within 24 months after the commissioner approves the assistance or invest at least \$25 million and create at least 200 new jobs within five years after the commissioner approves the assistance. Originally, the commissioner's authority to provide First Five assistance expired June 30, 2013. However, Public Act 13-247, Section 132, effective July 1, 2013, extended the commissioner's authority to June 30, 2015.

- **Public Act 12-147**, Section 10, effective upon passage, reassigned the responsibility for providing various administrative and support services for the quasi-public Capital Region Development Authority from the Office of Policy and Management (OPM) to DECD.
- **Public Act 12-183**, effective July 1, 2012, made programmatic and administrative changes to the DECD Brownfield Financing Program, which consists of separate grant and loan components. The act narrowed the range of entities eligible for assistance under both components, allowed loan proceeds to be used to develop housing meeting a broader range of needs, and allowed DECD to use a portion of program funds to cover staffing and marketing costs. The act also made procedural changes to the DECD Brownfield Liability Protection Program, which protects eligible property owners from liability to the state and third parties for cleaning up brownfields according to program requirements. It made changes to the process for accepting brownfields into the program, gave developers more time to pay program application fees, and reset the deadlines for completing specified tasks.
- **Public Act 13-234**, effective July 1, 2013, completed the establishment of DOH by giving DOH authority over state housing and community development programs and transferring to DOH housing-related responsibilities from other state agencies, including DECD.
- **Public Act 13-247**, Sections 244 to 248, effective July 1, 2013, created the Connecticut Arts Council within DECD to foster and support the arts.
- **Public Act 13-308**, effective July 1, 2013, consolidated and reorganized the laws governing DECD brownfield cleanup programs, making many programmatic and technical changes. It consolidated all DECD brownfield funds into a separate nonlapsing account and specified the types of funds that must be deposited in the account. The programmatic changes under the act included authorizing brownfield loans for reducing blight, narrowing the eligibility criteria for liability relief, and exempting private developers receiving financial assistance under the brownfield grant and loan programs from the statutory penalties for (1) relocating out of Connecticut within ten years after receiving assistance and (2) failing to create or retain the number of jobs stipulated in the assistance agreements.

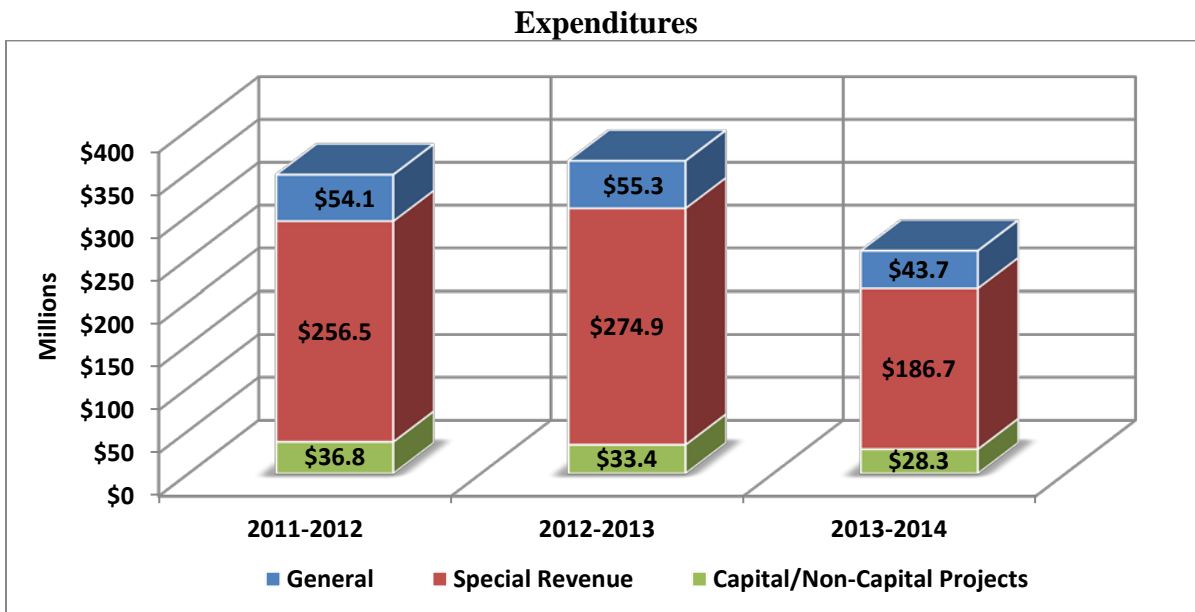
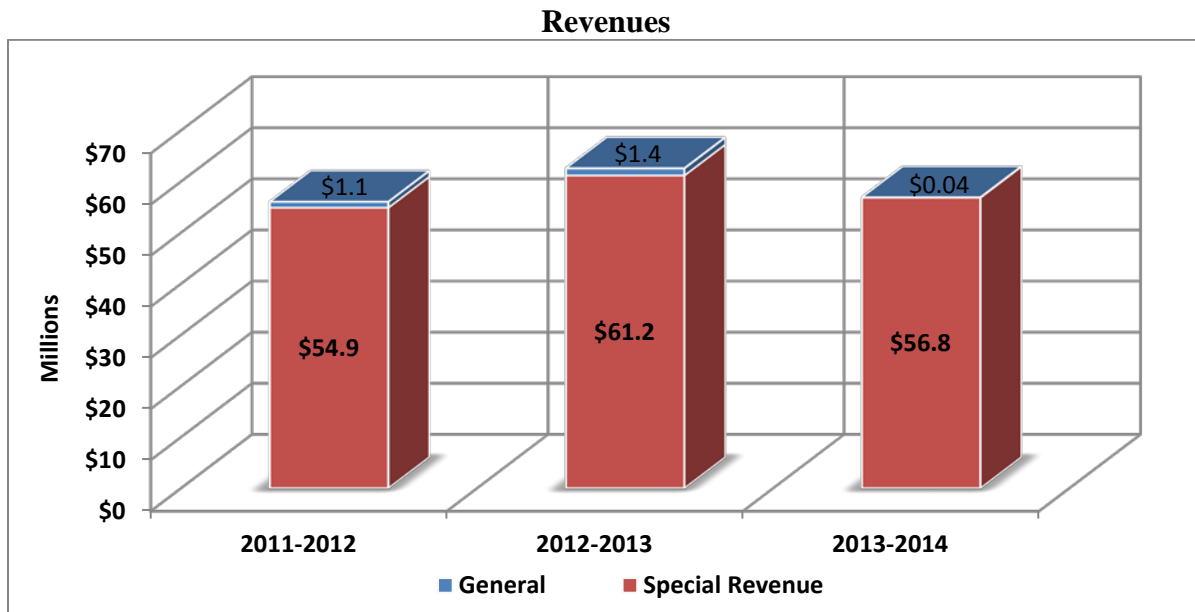
**Boards, Commissions, Committees and Councils**

Name	General Statute Section	Statutory Responsibilities
State Historic Preservation Board	§10-321q	To review recommendations by municipal preservation boards to the National Register of Historic Places and make recommendations that the DECD State Historic Preservation Officer either nominate or reject the proposed nominations.
Culture and Tourism Advisory Committee	§10-393	To advise DECD on the general powers, duties and functions related to enhancing and promoting culture, history, the arts and the tourism and digital media and motion picture industries in Connecticut.
Connecticut Arts Council	§10-408a and §10-408b	To foster and support the arts and manage the Connecticut Arts Council Foundation, which was established to raise funds from private sources to encourage participation in, and the promotion, development, acceptance and appreciation of, artistic and cultural activities.
Historic Preservation Council	§10-409	To advise DECD on critical historic preservation functions, review and approve requests to perform rehabilitation work on properties for which DECD holds preservation restrictions, prevent the unreasonable destruction of historic properties along with the assistance of the Office of the Attorney General, place and maintain suitable markers, memorials or monuments to designate sites or places of historical significance, and develop a model ballot for use by clerks of municipalities considering the establishment of local historic districts.
Sports Advisory Board	§10-425	To advise DECD on the most effective ways to utilize state resources to promote, attract and market in-state professional and amateur sports and sporting events and on ways to coordinate the use of state-owned facilities in order to enhance sports-related tourism in the state and develop methods for the dissemination of information concerning in-state professional and amateur sports and sporting events to residents of the state and the northeast.
Small Business Advisory Board	§32-9xx	To provide guidance to DECD with regard to resources available to small businesses.
Commission on Connecticut's Future	§32-245	To advise the General Assembly and DECD on issues related to defense conversion, industrial policy, and the state's business climate; evaluate legislation related to the state's economy, particularly as it affects manufacturers and defense-related businesses; provide a forum for business issues; stimulate and review public and private assistance to improve the state's economy; and prepare a report to the Governor and General Assembly concerning the economic renewal of Connecticut.

## RÉSUMÉ OF OPERATIONS

### Introduction

DECD operations for the fiscal years ended June 30, 2013 and 2014 were accounted for in the General Fund, special revenue funds, capital and non-capital improvement funds, and a trust fund. A summary of revenues and expenditures during the audited period and the preceding fiscal year for all funds, except the trust fund, follows:



The activity of each of the funds is presented in more detail in the sections that follow:



**General Fund**

A summary of General Fund receipts during the audited period and the preceding fiscal year follows:

Receipt Description	Fiscal Year Ended June 30,		
	2012	2013	2014
Energy Conservation Loan Interest	\$ 691,646	\$ 725,458	\$ -
Refunds of Expenditures	452,184	664,212	39,656
All Other	5,858	2,318	1,920
<b>Total Receipts</b>	<b>\$1,149,688</b>	<b>\$1,391,988</b>	<b>\$41,576</b>

The decrease in revenue in the fiscal year ended June 30, 2014 was primarily due to the transfer of housing-related programs to DOH.

A summary of General Fund expenditures during the audited period and the preceding fiscal year follows:

Expenditure Description	Fiscal Year Ended June 30,		
	2012	2013	2014
Personal Services	\$ 8,600,142	\$ 8,386,581	\$ 7,977,806
Other Expenses	1,020,457	1,045,971	629,471
State-Wide Marketing	12,519,911	11,611,421	12,016,248
Capital Region Development Authority	-	5,920,145	9,620,145
Other – Economic Development Grants	2,847,081	2,061,880	2,864,574
Theatre Grants	1,290,964	2,003,458	2,510,867
Culture, Tourism and Art Grant	1,879,618	1,949,219	-
Arts Commission	-	-	1,788,312
Tourism Grants	1,577,001	1,617,600	1,617,598
Other – Arts/Culture/Tourism	2,929,628	2,969,485	2,712,709
Other – Aquarium/Zoo/Museum Grants	1,923,437	1,923,430	1,959,339
Connecticut Humanities Council	2,049,752	-	-
Basic Cultural Resource Grant	1,510,328	-	-
Congregate Facilities	6,539,126	6,859,199	-
Elderly Rental Assistance	3,146,877	3,136,556	-
Payments in Lieu of Taxes	2,196,325	1,873,400	-
Assisted Living Demonstration	1,730,000	1,880,000	-
Tax Abatement	1,704,880	1,444,646	-
Other – Housing Assistance	678,213	661,796	-
<b>Total Expenditures</b>	<b>\$54,143,740</b>	<b>\$55,344,787</b>	<b>\$43,697,069</b>

The increase in total expenditures in the fiscal year ended June 30, 2013 was primarily attributable to administrative duties that were assigned to DECD pertaining to the Capital Region Development Authority (CRDA). The increase was partially offset by decreases resulting from the elimination of the requirement that the Connecticut Humanities Council operate in

conjunction with DECD, as well as the combining of the Basic Cultural Resource Grant with the Culture, Tourism, and Art Grant along with reduced appropriations for the combined grants.

The significant decrease in total expenditures in the fiscal year ended June 30, 2014 was primarily due to the transfer of housing-related programs and staffing to DOH. The decrease was partially offset with an increase due to additional funding received to support CRDA. It should be noted that funding from the Culture, Tourism and Art Grant account was transferred to the Arts Commission account upon the establishment of the Connecticut Arts Council.

### **Special Revenue Funds**

In addition to the fund used to account for federal and other restricted monies, DECD utilized 13 other special revenue funds during the audited period. These funds were used mainly for providing financial assistance in the form of grants or loans for economic development and housing projects approved by the State Bond Commission.

A summary of receipts from special revenue funds during the audited period and the preceding fiscal year follows:

<b>Receipt Description</b>	<b>Fiscal Year Ended June 30,</b>		
	<b>2012</b>	<b>2013</b>	<b>2014</b>
Federal Contributions	\$40,872,930	\$38,538,889	\$12,610,366
Restricted Contributions, Other	4,571,064	13,253,950	31,190,200
Principal and Interest on Loans	9,434,938	9,388,801	13,042,462
<b>Total Receipts</b>	<b>\$54,878,932</b>	<b>\$61,181,640</b>	<b>\$56,843,028</b>

The increase in total receipts in the fiscal year ended June 30, 2013 was primarily attributable to Community Investment Account distributions received for support of historic preservation activities pursuant to Section 4-66aa of the General Statutes, as well as grant transfers for the Small Business Express Assistance Account.

The decrease in total receipts in the fiscal year ended June 30, 2014 was primarily attributable to decreases in federal grants received for housing-related programs that were transferred to DOH. The decrease was partially offset by increases in grant transfers for Brownfield Remediation and Development and the Small Business Express Assistance Account.

A summary of expenditures from special revenue funds during the audited period and the preceding fiscal year follows:

<b>Expenditure Description</b>	<b>Fiscal Year Ended June 30,</b>		
	<b>2012</b>	<b>2013</b>	<b>2014</b>
Loans	\$148,918,608	\$154,736,571	\$89,083,111
Grants	100,041,679	109,805,469	88,767,674
Administration	7,567,874	10,347,259	8,874,071
<b>Total Expenditures</b>	<b>\$256,528,161</b>	<b>\$274,889,299</b>	<b>\$186,724,856</b>

Included in the above totals are federal and other restricted expenditures totaling \$61,305,023, \$46,579,099 and \$21,891,629 for the fiscal years ended June 30, 2012, 2013 and 2014, respectively. The transfer of housing-related programs to DOH resulted in the significant decrease in loans and grants for the fiscal year ended June 30, 2014. Fluctuations in loans and grants were mainly in the following funds: Economic Assistance Bond Fund, Economic Assistance Revolving Fund, Grants to Local Governments, Housing Assistance Fund, and Housing Trust Fund.

**Capital and Non-Capital Improvement Funds**

Total expenditures from capital and non-capital improvement funds were \$33,442,433 and \$28,281,985 for the fiscal years ended June 30, 2013 and 2014, respectively, compared to \$36,784,776 expended in the fiscal year ended June 30, 2012. Expenditures were made primarily from the Community Conservation and Development Fund under the Urban Act Program, under which funds are provided to municipalities, as well as non-profit and for-profit entities, to improve and expand state activities that promote community conservation and development and improve the quality of life for urban residents of the state.

**Connecticut Arts Endowment Fund**

The Connecticut Arts Endowment Trust Fund operates under the provisions of Sections 10-406 through 10-408 of the General Statutes. This fund is financed from the proceeds of state bonds that serve as the principal balance of the Arts Endowment Fund. The interest earnings for the current year become available for state matching grants to eligible arts organizations for the subsequent year. A summary of financial transactions for the audited period follows:

	<b>As of June 30,</b>		
	<b>2012</b>	<b>2013</b>	<b>2014</b>
Book Value, beginning of year	\$15,384,894	\$15,328,883	\$16,524,359
Shares Purchased	822,319	8,641,345	1,363,957
Shares Redeemed	(872,152)	(8,761,988)	(1,728,528)
Gains/(Loss) on Shares Redeemed	(6,178)	1,316,119	160,720
Net Investment Income Earned	620,700	500,064	135,496
Net Investment Income Distributed	(620,700)	(500,064)	(135,496)
<b>Book Value, end of the year</b>	<b>\$15,328,883</b>	<b>\$16,524,359</b>	<b>\$16,320,508</b>

The fair market value of trust fund assets at June 30, 2014, was \$19,046,210.

## STATE AUDITORS' FINDINGS AND RECOMMENDATIONS

The following reportable matters resulted from our review of the records of the Department of Economic and Community Development (DECD).

### **Cash Management**

*Background:* DECD disburses grant funds for housing and economic development programs. Assistance agreements between the department and its grantees require the grantees to submit audit reports to the department. After DECD reviews the audit reports and is satisfied with the accuracy of the total grant expenditures, it issues a Certificate of Approved Program Cost and State Funding, which summarizes DECD payments to the grantee for the specific project, total expenditures, any adjustments, and the amount due to or from DECD. DECD then bills the grantee for any amounts due.

Effective July 1, 2013, Public Act 13-234 transferred various housing-related responsibilities from DECD to the newly established Department of Housing. Since the majority of amounts due to DECD during the audited period pertained to housing-related programs, audit testing focused on amounts due prior to the transfer of the programs.

*Criteria:* Cash management procedures should ensure that payments to grantees are based on immediate needs and refunds of overpayments are received as soon as possible.

*Condition:* As in our prior audits, we noted that DECD cash management procedures appear in need of improvement. During the period beginning July 1, 2012 through June 30, 2013, DECD issued 166 Certificates of Approved Program Cost and State Funding that reflected amounts due to DECD totaling \$685,625.

The length of time that grantees held unexpended state funds before returning them to DECD seems excessive. For the 15 projects we reviewed, the time between the last DECD payment and receipt of a refund was less than one year for two projects, one to two years for nine projects, and two to three years for four projects. The four refunds due over two years amounted to \$73,052.

*Effect:* DECD grantees received funding in excess of their needs and did not return those excess funds to DECD in a timely manner.

*Cause:* DECD did not ensure that grantees only received amounts necessary to meet the cash needs of the funded project or that refunds of overpayments were received in a timely manner.

The assistance agreements are worded in a way that the grantees owe refunds to DECD after the certificate is issued. The grantee does not have the responsibility for refunding DECD at the end of the budget period or upon project completion.

DECD informed us that instead of receiving a return of funds, it is easier for it to allow the grantees to hold the funds, and to suggest to the grantees that they may consider expanding the funded project with those DECD funds or use the funds for another project. This circumvents the established procedures for processing applications and reviewing payments to grantees.

*Recommendation:* The Department of Economic and Community Development should improve its cash management procedures by only disbursing funds for immediate needs and reducing the time to collect refunds of overpayments. Rewording of assistance agreements should be considered to require more timely refunds. (See Recommendation 1.)

*Agency Response:* “The department does not agree with this finding.

DECD funds a variety of projects that include multi-million dollar construction, infrastructure improvements, acquisition of equipment, training and other activities. These projects can take several months or even years to complete. Because of recipients’ scheduling requirements, funds may be advanced based on the projected schedule to ensure timely payment to vendors and maintain project schedules. When funds are advanced for a short-term need, the advance is based on the eligible expenditures being funded by a particular program. A second advance will not be approved by DECD until the client has provided documentation that the initial advance has been expended or specified milestones are reached.

There are certain programs that require an applicant to match state financing with other sources of funds that may be provided to a project over the entire budget period, which may take longer to expend. In those cases DECD cannot perform a financial closeout of the project until project completion. It would then be determined if funds were due back to DECD.

DECD considers requests to reallocate remaining funds to activities that are related to the original scope of a project. DECD would not allow funding recipients to retain funds for a new project that has not been reviewed or approved. Any new project would require review and appropriate approvals. Bond Commission approval may be also required.

The department recognizes that on occasion, it takes a long period of time to obtain the return of funds by clients. The department also recognizes that there are no established legal or regulatory requirements that unused state funds must be returned within a certain time period. Therefore “timely” becomes a matter of interpretation or circumstance. However, the department does ensure that funds owed to the state are returned. The department believes that its cash management system provides reasonable assurance that excessive funds are not disbursed, and that clients provide refunds to the state as soon as practicable depending on the needs of the project.”

*Auditors’ Concluding*

*Comments:* We consider a period of over one year to three years to be excessive for the refund of monies owed to the state. For 13 of the 15 projects reviewed, funds were not refunded to the state until over one year later.

**Monitoring of Unused Bond Allocations**

*Background:* DECD finances a variety of economic, housing and community development projects using state bond funds approved by the State Bond Commission. The State Bond Commission requires that all unused balances from prior approvals be returned to the unallotted balance under the fund and section of origin once a project is completed or cancelled.

*Criteria:* Written policies and procedures for bond-funded projects should include procedures to monitor unexpended balances from bond-funded projects that are completed or cancelled.

*Condition:* In prior audits, we found that DECD had not implemented formal policies and procedures to address the administration of unexpended balances on bond-financed projects. Our current review revealed that this condition has continued.

*Effect:* The lack of fully-implemented written procedures for monitoring unexpended balances on bond-funded projects lessens the department’s assurance that unused bond funds are being returned to their original funding source in a timely manner.

*Cause:* DECD drafted policies and procedures that were approved by the commissioner during May 2014, but were only partially implemented beginning in March 2015.

*Recommendation:* The Department of Economic and Community Development should fully implement formal policies and procedures to ensure that unused balances from prior State Bond Commission approvals are identified in a timely

manner and returned to the unallotted balance under the fund once a project is completed or cancelled. (See Recommendation 2.)

*Agency Response:* “The department agrees with this recommendation. Implementation of the formal policy and procedure was completed on July 1, 2015. Unused balances are identified, unallotted and returned to available reserves when a project is completed or cancelled.”

### **Ineffective Receivables Reconciliation Processes**

*Background:* Each year, DECD reports its June 30<sup>th</sup> receivable balances to the State Comptroller. Balances reported include grant overpayments and Energy Conservation Loan (ECL) receivables serviced by a private contractor.

Effective July 1, 2013, Public Act 13-234 transferred various housing-related responsibilities from DECD to the newly established Department of Housing. Since the grants and ECL receivable amounts reported pertain to housing-related programs, audit testing consisted of the receivable amounts as of June 30, 2013.

*Criteria:* An adequate system of internal controls should include annual reconciliations of beginning balances, activity and ending balances. Reconciliations should identify any errors or improper entries made to receivable balances so corrections and accurate reporting can be performed.

Entities reporting loan receivables administered by third-party loan servicers should ensure that reported amounts reflect loan receivable balances carried by the loan servicer. Sound internal controls provide for the receipt of a report on internal controls (SOC 1) at the service organization. Statement on Standards for Attestation Engagements No. 16 (SSAE 16), issued by the American Institute of Certified Public Accountants (AICPA), is in effect for periods ending on or after June 15, 2011. This standard exists to report whether proper internal controls are in place at private entities providing contracted services for state programs.

*Condition:* Grant Refunds  
Reconciliations of grant refund activity and reported receivable balances were not performed. A receivable balance of \$1,121,479 existed as of June 30, 2013.

ECL Loans  
The ECL program balance reported as of June 30, 2013 was \$9,752,647. Although DECD attempted monthly reconciliations of ECL principal

balances to amounts reported monthly by the loan servicer, these reconciliations included unresolved items.

Although DECD has received reports of a limited review of its loans with the ECL servicer under an agreed-upon-procedures review, DECD did not require that the ECL servicer provide a report on its controls pursuant to SSAE 16.

*Effect:* Loans administered by a third-party servicer may not be properly accounted for or reported. Financial disclosures on the state's financial statements may be inaccurate.

*Cause:* Grant Refunds  
Reconciliations of receivables were apparently not considered.

ECL Loans  
Unreconciled amounts have not been addressed and resolved.

DECD receives annual audit reports from the ECL servicer. However, those audit reports do not specifically identify DECD funding. DECD did not require SSAE 16 reviews of the loan servicer.

*Recommendation:* The Department of Economic and Community Development should perform complete reconciliations of receivable activity and balances before reporting balances to the State Comptroller.

For Energy Conservation Loan balances, DECD should attempt to reconcile the differences between the loan servicer and DECD amounts. DECD should require a report prepared pursuant to Statement on Standards for Attestation Engagements No. 16. (See Recommendation 3.)

*Agency Response:* "The department agrees with the findings regarding reconciliation.

DECD has initiated work on the reconciliation of receivables activity and balances for Energy Conservation loans. Reconciliation of this account requires an extensive commitment of time by a qualified accountant. Completion of the reconciliation process has been slowed by staff turnover and restrictions on hiring qualified personnel.

Responsibility for the Energy Conservation Loan program was transferred to DOH on July 1, 2013. DOH considered requiring their loan provider to provide an SSAE 16 report. This report is not required by statute or regulation. DOH decided not to include this requirement in the contract with the service provider because of the burdensome cost it would create for the provider."



*Auditors' Concluding*

*Comments:*

The usefulness of the SOC 1 Report should be more carefully considered for ensuring both the effectiveness of the service organization's internal controls and the accuracy of the state's financial statements. The department should also consider whether the benefits of the report would outweigh the financial burden relative to the amount of loans administered and the administrative fees paid to the service organization.

**Erroneous Loan Interest Receivable Balances**

*Background:*

Section 32-1c subsection (b) allows DECD to provide financial assistance to organizations for planning and other functions pertinent to economic development. Financial assistance shall be rendered upon such contractual arrangements as may be agreed upon by the commissioner and any such organization in accordance with its respective needs.

In order to support the growth and innovation of Connecticut business, DECD administers a number of financing programs to assist businesses. DECD assistance agreements with recipients stipulate the terms and conditions of the assistance provided, including any interest or penalties that could be assessed. Executed loans are entered into and maintained on the department's loan management system, which automatically generates monthly invoices detailing principal and interest amounts.

Each year, DECD reports its June 30<sup>th</sup> receivable balances to the State Comptroller, which includes loan interest and late fee receivables based on reports from the loan management system. The State Comptroller includes reported amounts in the state's Comprehensive Annual Financial Report (CAFR).

*Criteria:*

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

Good business practice dictates that interest receivable on loans should be accrued and billed to borrowers properly and in accordance with agreed-upon contractual arrangements.

*Condition:*

DECD reported receivables for interest and late fees of \$5,531,084 and \$3,352,373, for the fiscal years ended June 30, 2013 and 2014, respectively. Testing of the reported receivable balances disclosed understated interest receivables for 18 loans totaling \$4,882 and overstated interest receivables for one loan amounting to \$41,789.

*Effect:* Interest accruals in the loan management system did not always agree with the amounts billed to recipients and were not always calculated in accordance with the terms of the assistance agreements, resulting in different (generally lower) interest amounts being charged than stipulated in the agreements. Furthermore, interest receivable amounts reported to the State Comptroller were not accurate.

*Cause:* The understatements were due to the incorrect setup of the interest calculation methods in the loan management system, as well as discrepancies in the assistance agreements on how to calculate and bill interest. Further review disclosed that 146 loans, amounting to nearly \$109 million, were set up incorrectly in the loan management system.

The overstatement occurred with a loan requiring two separate accrual periods, for which the dates of the accrual periods in the loan management system overlapped, duplicating interest receivables.

*Recommendation:* The Department of Economic and Community Development should ensure the proper calculation of loan interest receivables and consistency with the amounts billed to recipients in accordance with financial assistance agreements. (See Recommendation 4.)

*Agency Response:* “The department agrees with this finding. The incorrect interest calculations resulted from the manner in which loans were setup in the Nortridge loan software. Beginning in May 2013, all loans are setup using templates thus ensuring that interest calculations are correct. Supervisory staff reviews all loan setups and staff received onsite training from the software vendor. Interest calculations for loans that were set up prior to that date are being reviewed individually and corrected as appropriate. The department expects the review process to be completed during fiscal year 2016.”

### **Unauthorized Earning of Overtime and Compensatory Time**

*Criteria:* Section 5-245 of the General Statutes provides that employees receive overtime pay for a period in addition to the hours of the employee's regular, established workweek when the work performed is authorized by the employee's appointing authority.

Collective bargaining agreements permit agency employees to earn compensatory time, with prior supervisory approval, for time worked in excess of their normal work schedule.

DECD policies and procedures require that compensatory time and overtime must be authorized in advance by the office/unit administrator

and commissioner. Written approval must be obtained at least 24 hours in advance using the appropriate request form.

*Condition:* A review of overtime paid to five employees during the audited period, which consisted of 173 instances totaling 648 hours, disclosed that proper authorization was not obtained in eight instances totaling 39 hours.

A review of compensatory time earned by five employees during the audited period, which consisted of 160 instances totaling 870 hours, disclosed that proper authorization was not obtained in 40 instances totaling 188 hours.

*Effect:* Employees were paid overtime and earned compensatory time without prior authorization.

*Cause:* Administrative controls over the earning of overtime and compensatory time were inadequate.

*Recommendation:* The Department of Economic and Community Development should ensure that overtime and compensatory time is properly approved within the required timeframe. (See Recommendation 5.)

*Agency Response:* “The department agrees with the finding. DECD policy which requires that compensatory and overtime be authorized in writing 24 hours in advance has been re-communicated to all employees. Procedures have been reviewed and strengthened. Monitoring will be enhanced by having directors notified in the event that overtime and compensatory time is submitted on timesheets without the required prior authorization.”

### **Longevity Payment Errors**

*Criteria:* Section 5-213 of the General Statutes authorizes the payment of semiannual longevity payments to state employees who are included in a collective bargaining unit and have completed ten years of state service. Payments are made in accordance with longevity rate schedules established by the Department of Administrative Services. Payments increase after employees complete 15, 20, and 25 years of state service.

An agreement between the State of Connecticut and the State Employees Bargaining Agent Coalition, known as the SEBAC 2011 Agreement, states that, for current employees hired prior to July 1, 2011, no service shall count toward longevity for the two-year period beginning July 1, 2011 through June 30, 2013. Effective July 1, 2013, any service accrued during that period shall be added to their service for the purpose of

determining their eligibility and level of longevity entitlement if it would have counted when performed.

*Condition:* Our review of longevity payments during the audited period disclosed that two employees received payments prior to attaining ten years of state service.

*Effect:* Employees received longevity payments that they were not entitled to.

*Cause:* The department misinterpreted the language of the SEBAC agreement to signify that, since the two employees were hired prior to July 1, 2011, they continued to be eligible for longevity payments and the stipulation that no service shall count toward longevity during the period covered by the agreement did not apply.

*Recommendation:* The Department of Economic and Community Development should ensure the correct recording and accrual of state service time eligible towards longevity to ensure that longevity payments are made in accordance with state statutes and collective bargaining agreements. (See Recommendation 6.)

*Agency Response:* “The department agrees with this finding. The required process to execute payroll adjustments for the two employees involved has been initiated.

In October 2013, DECD’s payroll processing was transferred to the Department of Administrative Services (DAS) SmART unit. The SmART unit maintains personnel spreadsheets that are compared to CORE in April and October to ensure that employees are paid correctly.”

### **Reporting in Accordance with Travel Policies**

*Criteria:* On February 9, 2011, the Governor modified the out-of-state travel ban that had been in effect since May 2008, and directed that out-of-state travel only be allowed if approval was given by agency heads and one of the following criteria were met:

- Travel is to pursue economic development opportunities or secure significant outside funding for the state;
- Travel will enable the state employee or official to protect, promote or gather information related to critical state policies and alternative means of gathering information when web-based or internet attendance is not available; and
- Non-state funds are used to cover the entire cost of the trip.

Agency heads are responsible to review out-of-state travel requests in accordance with this directive as well as other applicable state criteria. To ensure compliance with this directive, agencies are required to submit a monthly out-of-state travel report to the Office of Policy and Management (OPM) Budget Division.

*Condition:* The department's out-of-state travel reports submitted to OPM for the period beginning July 1, 2013 through June 30, 2014 identified a total of 90 out-of-state trips during the period. Our review of the department's supporting documentation for out-of-state travel during the period revealed an additional eight trips that were not reported to OPM in accordance with the Governor's directive.

*Effect:* The department was not in compliance with the Governor's directive regarding out-of-state travel reporting.

*Cause:* The failure to properly report all instances of out-of-state travel was due to oversights by staff.

*Recommendation:* The Department of Economic and Community Development should ensure that all out-of-state travel is properly documented, authorized, and reported. (See Recommendation 7.)

*Agency Response:* "The department agrees with this finding. This finding resulted from reports submitted by a single employee who is no longer employed with the department. A tracking mechanism has been implemented to prevent re-occurrence and out-of-state travel is being consistently reported to OPM."

### **Obligations Incurred Without Proper Accounting Commitments**

*Criteria:* Section 4-98(a) of the General Statutes states that no budgeted agency may incur any obligation except by the issuance of a purchase order and a commitment transmitted to the State Comptroller.

Proper internal controls related to purchasing require that commitment documents be properly authorized prior to the receipt of goods or services.

*Condition:* In our reviews of a total of 108 expenditure transactions during the audited period, we noted that 47 purchase orders were created and/or approved after the receipt of goods or services and three expenditures were made without the issuance of a purchase order.

*Effect:* When obligations are incurred without the proper commitment of funds, there is less assurance that funding will be available at the time of payment.

*Cause:* We were informed that, for grant and loan transactions, program staff approve assistance agreements and payment requests before providing the department's Office of Finance and Administration all the information necessary to prepare the purchase orders.

*Recommendation:* The Department of Economic and Community Development should strengthen its internal controls to ensure that funds are committed prior to purchasing goods and services. (See Recommendation 8.)

*Agency Response:* "The department acknowledges the importance of internal controls regarding the commitment of funds prior to purchasing goods and services.

We note that no grant or loan payments were made without properly executed contracts and budget documents. With regard to grant and loan payments, this finding resulted from payment requests being submitted at the same time as other contract documents. A revised procedure for the submission of payment requests has been implemented. Project managers are now required to submit contract documents and receive a purchase order number **prior** to signing and submitting a payment request.

All staff has been instructed regarding the necessity of obtaining approvals and purchase orders in advance of purchasing goods and services. DECD's Office of Finance and Administration is closely monitoring all purchases to be sure that POs are properly issued in advance and corrective action is taken when appropriate."

### **Lack of Disaster Recovery Plan**

*Criteria:* Sound business practices include provisions that organizations have a current information technology (IT) disaster recovery plan in place to enable critical operations to resume activity within a reasonable period should a disaster or major interruption in IT systems occur.

*Condition:* During the audited period, DECD did not have a current comprehensive IT disaster recovery plan in place documenting recovery and testing strategies related to its existing IT infrastructures. In addition, no provisions have been made for a backup site or computer hardware and software.

*Effect:* The lack of a current IT disaster recovery plan and provisions for a backup site or computer hardware and software reduces the likelihood of resuming critical operations in a timely manner in the event of a disaster or major interruption of the department's IT systems.

*Cause:* Although the department has taken steps to improve its IT infrastructure, including the development of data recovery strategies and the implementation of testing procedures, a current IT disaster recovery plan has not been developed, nor have all contingency provisions been established.

*Recommendation:* The Department of Economic and Community Development should continue its efforts to develop a current comprehensive information technology disaster recovery plan, including the proper coordination and periodic testing of contingency provisions within the plan. (See Recommendation 9.)

*Agency Response:* “The department disagrees with this finding and notes that substantial efforts that have been made in this area.

A Disaster Recovery plan was developed and implemented on March 4, 2012 which identified responsibility for critical systems procedures and contingencies in the event of a disaster which incapacitated DECD’s systems. A full system backup (of production data and system files) to tape is performed on a scheduled basis. Tapes are rotated to a secure off-site location.

DECD implemented two (2) high-end servers within a virtualized environment. Disaster recovery testing was performed in February 2015 and all agency servers tested successfully from back-up tapes.

The department has initiated a move of all applications to the BEST data center. The move to BEST management of servers will provide a cost-effective environment for data protection, testing, and disaster recovery.”

*Auditors’ Concluding  
Comments:*

The Auditors of Public Accounts acknowledge the improvements made by DECD related to its IT infrastructure, however, the plan implemented on March 4, 2012 was outdated and incomplete because it did not document the strategy of testing performed by DECD during February 2015, the current recovery strategies as of the date of audit testing during July 2015, and provisions for a backup site to ensure that critical operations are resumed in a timely manner should such an event occur.

### **Incomplete Inventory Reporting and Insufficient Internal Controls**

*Background:* Pursuant to Public Act 11-48, effective July 1, 2011, DECD assumed the responsibilities of the Connecticut Commission on Culture and Tourism (CCT), including the transfer of functions, duties, personnel, obligations, also including but not limited to, the transfer of records and property.

There are four state-owned museums operated by the DECD State Historic Preservation Office. Each museum's collection is recorded in a separate and specially designed database system, which museum staff is responsible for maintaining. In addition, the museums feature gift shops in which visitors can purchase souvenir items.

*Criteria:*

Section 4-36 of the General Statutes requires each state agency to establish and keep an inventory account in the form prescribed by the State Comptroller and to submit an annual report to the State Comptroller of its inventory balances.

The State Property Control Manual specifies requirements and standards that a state agency's property control system must include to ensure that all assets owned by or in the custody of the state are properly recorded and reported, including that only capitalized assets (individual assets with a value or cost over \$1,000) are reported on the Asset Management/Inventory Report (CO-59 form). The report must be submitted by October 1<sup>st</sup> and must reflect the sum total of the physical inventory as of June 30<sup>th</sup>.

Furthermore, the manual prescribes that museum collections are part of historical treasures and reported as art on the CO-59 form. These items must be maintained in a separate inventory account for each item regardless of cost or value. Items valued over \$1,000 should be included on the CO-59 form.

The department's own collection management policies also state that all acquisitions shall remain in art collections as long as they retain their physical integrity, authenticity, and usefulness within the objectives and purposes of the collections. All artifacts are subject to rules of the state, including inventory control procedures.

*Condition:*

DECD did not submit the CO-59 form for the fiscal year ended June 30, 2013 until May 10, 2014, which was seven months late.

All four museums' reportable collections were still not accurately reported on the CO-59 form. One museum collection was based on values from an appraisal performed in 2008, which included items that were returned to owners and were no longer in the possession of the museum.

The museums' gift shop inventories reported for the fiscal year ended June 30, 2013 included only one of the four museums' inventories. Although all four museums' inventories were reported for the fiscal year ended June 30, 2014, the ending balance was understated by \$7,427 as a result of a calculation error related to one of the museums.



*Effect:* Reported amounts were not complete and accurate, and DECD was not in compliance with the requirements of the State Property Control Manual.

*Cause:* We were informed that, due to the consolidation with CCT, DECD still had difficulty reconciling the additional inventory reported against the supporting documentation provided. In addition, without providing the value of each item in the museum collections on the inventory list provided by the CCT offices, DECD was unable to determine the amounts to report for the museum collections.

*Recommendation:* The Department of Economic and Community Development should improve internal controls over asset accountability and reporting to ensure compliance with the requirements of the State Property Control Manual. (See Recommendation 10.)

*Agency Response:* “The department agrees with this finding. Corrective action has been taken as follows:

CO-59s for FY 14 and FY 15 were submitted on time and included accurate reporting of museum gift shop inventories. Staff has received training in accurate completion of the CO-59 and a tracking mechanism was initiated for timely submission of the CO-59.

In August 2014 a professional appraisal of the museums’ collections was completed and the appraised values were reported via the CO-59. A professional appraisal will be obtained every five years as recommended, resources permitting.”

### **Deficiencies in Controls over Physical Assets**

*Background:* Pursuant to Public Act 11-48, effective July 1, 2001, DECD assumed the responsibilities of the Connecticut Commission on Culture and Tourism (CCT), including the transfer of functions, duties, personnel, obligations, also including but not limited to, the transfer of records and property.

There are four state-owned museums operated by the State Historic Preservation Office of DECD. Each museum’s collection items are recorded in a separate and specially designed database that museum staff is responsible for maintaining.

*Criteria:* Section 4-36 of the General Statutes requires each state agency to establish and keep an inventory account in the form prescribed by the State Comptroller and to submit an annual report to the State Comptroller of its inventory balances.

The State Property Control Manual specifies requirements and standards that a state agency's property control system must include to ensure that all assets owned by or in the custody of the state are properly acquired, managed and disposed of, including that agencies:

- Ensure the maintenance of complete and accurate property records utilizing the Core-CT Asset Management Module. Proper internal controls dictate that property control records contain certain information to adequately record and track equipment items. At a minimum, this information should include item description, cost, tag number, and location;
- Assign a tag to each asset that provides a unique identification number and the property owner's name (i.e., state agency);
- Perform a complete physical inventory of all property by the end of each fiscal year to ensure that property control records accurately reflect the actual inventory on hand; and
- Continuously survey property to determine which assets are no longer needed, reassign property among its activities when it is no longer required for its current use, and report to the Connecticut Property Distribution Center personal property that becomes surplus to an agency's needs, is unserviceable, obsolete, or otherwise unusable.

*Condition:*

We reviewed a total of 50 assets, 15 selected from a Core-CT Capital Asset Report, ten selected from a Core-CT Capital Asset Expenditure Report, and 25 selected during a physical inspection of the department's tagged assets. Our review disclosed the following deficiencies:

- One item could not be located at the department;
- Six items were found in locations other than indicated in Core-CT;
- One item was physically inspected at the agency although it was indicated as disposed in Core-CT;
- One item had both DECD and CCT identification tags attached but was recorded in Core-CT under the former CCT tag rather than the current DECD tag. Additional inspections of assets at the department's Constitution Plaza location revealed numerous other items with both tags attached. Reviews of some of these tag numbers in Core-CT disclosed inconsistencies pertaining to which tags were used for recording purposes. However, it seemed that most were still recorded under the CCT tag; and

- Ten items appeared to no longer be in use for quite some time but were listed as in service in Core-CT.

Additional inspections of assets on the agency's premises noted numerous items that no longer seemed required for use, yet no steps had been taken for their proper disposition. Most noteworthy were 92 older computers, with a combined historical cost in Core-CT of over \$80,000, which were observed in a storage room. The majority of these computers' locations have not been updated in Core-CT since April 2014, giving us further reason to believe that no action was taken to dispose of them. In addition, during a physical inspection of items at the department's Constitution Plaza location, we observed a significant amount of unused equipment in unoccupied cubicles.

A review of 15 assets that were either transferred to other state agencies or scrapped per Connecticut Property Distribution Center reports disclosed that four items were not properly deleted from Core-CT and were observed during a physical inspection.

Our review of the Core-CT Physical Inspection Report indicated that not all of the department's assets were physically inspected during fiscal year 2013-2014 and that no physical inspections of the museums' collection items were conducted.

Museum collections are recorded in the PastPerfect system, which is specially designed to record museum collections. They are not reflected on the Core-CT Asset Management module. However, due to a lack of supporting documentation, we are unable to determine whether each item is recorded in accordance with the manual, which specifies the minimum data required for a property control record. In addition, we were informed that not every collection item is recorded in the system.

*Effect:* Deficiencies in internal controls over equipment inventory result in a decreased ability to properly safeguard assets and decrease the accuracy of financial reporting.

*Cause:* The property control system is not completely maintained as required by the State Property Control Manual. Furthermore, the department did not fully complete the physical inspection of all property to ensure that property control records accurately reflect inventory on hand.

*Recommendation:* The Department of Economic and Community Development should ensure the proper maintenance and control of its assets with detailed records, including tag numbers. Furthermore, the department should continuously survey its inventory levels and perform complete annual physical inspections. (See Recommendation 11.)

*Agency Response:* “DECD agrees that it should ensure all offices maintain and control assets with detailed records. We note however, that this task has been complicated by CT Commission on Culture and Tourism (CCT) assets, including extensive museum holdings, being brought into DECD, and the need to transfer assets to DOH. Competing priorities for decreased staff resources have limited DECD’s ability to update CORE and dispose of assets via the lengthy surplus process.

**Assets no longer in use:** DECD disagrees that the 92 computers which needed to be discarded via the surplus process had a value of \$80,000. Despite the listed value in CORE, these units were obsolete and had minimal, if any, value. They have been disposed of via the surplus process. The unused equipment observed in unoccupied cubicles at DECD’s Constitution Plaza Office, was the property of Department of Labor (DOL). After repeated requests, DOL has removed their items. An initiative to identify all assets no longer in use, dispose of them through the surplus process and update the records in CORE has been initiated and we expect the surplus process to be completed prior to filing the FY16 CO-59.

**Physical inspections** were conducted during 2013-2014, however DECD acknowledges that they were not properly recorded in CORE. The agency has undertaken a physical inspection of all assets in its facilities that will include updating assets tags, transferring assets to DOH and updating entries in CORE.

**Museum Collections:** DECD notes that all museum collection items were recorded in an object file (paper). All items in museum collections at Whitfield, Prudence Crandall and Eric Sloan museums have been entered into PastPerfect, a software system designed to track museum holdings. Additional details (such as dimensions) are being entered as resources allow. Data entry is hindered by the large number of collection items (Henry Whitfield Museum’s collection alone exceeds 10,000 items) and limited staffing. Laptops are being purchased and an upgrade of PastPerfect software will facilitate data entry. The remaining required information is expected to be entered by the end of 2017.

Collection items at the Old New-Gate Prison & Copper Mine have not been entered into PastPerfect due to closure for renovations. As soon as the site is staffed, a target completion date for entry into PastPerfect will be determined.”

*Auditors’ Concluding  
Comments:*

Although the 92 computers may not have had a significant current value, \$80,000 was the amount at which the assets were valued in Core-CT and reported to the State Comptroller as capitalized inventory.

Regarding the unused equipment inspected in the DECD Constitution Plaza Office, our observation concluded that the assets did consist of items belonging to both DECD and DOL.

### **Inadequate Documentation of Monitoring – Housing Programs**

*Criteria:* Assistance agreements between DECD and recipients of Small Cities Community Development Block Grants (Small Cities) require municipalities to submit progress and status reports to DECD. According to the department’s Small Cities Grant Program Management Manual, the 1<sup>st</sup> and 3<sup>rd</sup> quarter reports are due five days after the end of the quarter and the 2<sup>nd</sup> and 4<sup>th</sup> quarter reports are due 15 days after the end of the quarter. However, DECD allows the municipalities 30 days after the end of the quarter to submit the reports.

The manual also provides that DECD will conduct on-site monitoring at least once during the time period of a Small Cities grant. Once completed, a monitoring letter is sent to the municipality indicating whether the municipality complied with statutory and regulatory requirements. For instances of noncompliance resulting in a finding, the municipality must respond within 30 days of the date of the letter with a corrective action plan. The plan must be implemented within 60 days of the letter.

Furthermore, the manual requires DECD to initiate close-out procedures for Small Cities projects when it is determined that all costs to be paid with grant dollars should have been incurred. DECD will issue a certificate of completion if an audit, in accordance with Single Audit Act requirements, was completed and accepted by DECD; the grantee submitted a final quarterly report; and DECD monitoring of grantee files determined that all laws and regulations have been met.

DECD requires the completion of an eligibility review form to properly assess program eligibility for HOME Investment Partnerships (HOME) and Affordable Housing (FLEX) projects.

Assistance agreements between DECD and recipients of HOME and FLEX program funding require that borrowers/grantees provide the following to DECD:

- Semi-annual project financing statements within 30 days after June 30<sup>th</sup> and December 31<sup>st</sup> until the expiration date of the development budget;

- Quarterly milestones and progress reports no later than 30 days after the end of each quarter until the expiration of the development budget; and
- Cost certifications within 60 days of substantial completion of the project or at such times as required by the commissioner.

The department's HOME Compliance Manual provides that DECD will conduct on-site program monitoring visits of each owner at least once every two years after project completion during the compliance period, and that a follow-up monitoring letter will be issued within 30 days from the date of the visit to inform the owner of the monitoring results. If concerns, deficiencies, or findings are identified, the owner should take steps to resolve them and respond to the letter within 30 to 60 days.

The department's Internal Process Manual provides that HOME project monitoring must occur after projects are completed. Projects are considered completed when all funds are expended, construction is completed, and the project is occupied.

*Condition:*

A review of five Small Cities project files identified the following deficiencies:

- Four projects were missing quarterly progress reports; and
- For two projects, DECD did not issue monitoring letters and certificates of completion to the municipalities in a timely manner after the project periods ended and monitoring was conducted. The letters and certificates were not issued as of the date of our audit on April 30, 2015, which was over one year after the project periods ended and monitoring was conducted.

A review of five HOME project files and five FLEX project files identified the following deficiencies:

- Three FLEX projects were missing eligibility review forms;
- One HOME and three FLEX projects were all missing required semi-annual project financing statements;
- Three HOME and three FLEX projects were missing quarterly progress reports or reports were submitted to DECD up to 20 months after they were due;

- Five HOME and three FLEX projects did not have cost certifications submitted to DECD within 60 days of substantial completion. The certifications were submitted up to 26 months after they were due;
- One HOME project did not have program monitoring results sent to the owner within 30 days of the monitoring visit. The letter was not sent until three months after it was required; and
- Two HOME projects did not have project monitoring performed in a timely manner. For one project, monitoring was not performed until 28 months after the project was considered complete. For the other project, monitoring was not performed as of the date of our audit on April 30, 2015, which was 21 months after the project was considered complete.

*Effect:* The department’s ability to determine potential project eligibility and monitor project performance and allowable expenditures is impaired if the proper forms are not completed and obtained in a timely manner.

Inappropriate payments may be made if periodic reports are not obtained and reviewed when required. Excess disbursements made by the department may not be identified and returned in a timely manner.

*Cause:* A lack of attention to recordkeeping and a disregard for and lack of enforcement of assistance agreement requirements appeared to have caused the conditions.

*Recommendation:* The Department of Economic and Community Development should ensure that assistance agreement requirements and internal control policies are followed. (See Recommendation 12.)

*Agency Response:* “As of July 1, 2013 responsibility for these programs was transferred to the Department of Housing (DOH).

*DOH Response:* The department partially agrees with these findings.

**Small Cities Community Development Block Grant:** Although the department recognizes that it would be preferable to complete monitoring and issue certificates of completion more quickly, it is neither a contractual nor regulatory requirement to do so within a specific timeframe. In addition, the characterization of four missing quarterly reports out of those projects that were characterized as either a “lack of attention to recordkeeping” or “lack of enforcement of assistance agreement requirements” is not accurate.

The department continues to take its monitoring and close out responsibilities seriously, and will continue to work with our grantees to ensure that proper reporting is completed.

**HOME Investment Partnerships Program and the Affordable Housing (FLEX) program:** The department has revised the semi-annual project financing statement reporting requirements to make submission of these financial statements optional, at the Commissioner’s discretion. This change in policy, although not reflected in the older assistance agreements, is the standard procedure that is currently being followed. This change is a direct result of the department’s efforts to LEAN all of its processes. These new requirements, although not reflected in the original documents, have been implemented to better reflect current processes and conditions. The department has taken prudent steps to operate more effectively and efficiently.

**Eligibility review form for FLEX applications** is used to review all housing development applications and has been expanded to include both the HOME and FLEX/HTF eligibility. This has eliminated any issues with regard to eligibility for these programs. It should also be noted that of the ten (10) files reviewed, there were no instances of ineligibility identified for either HOME or FLEX funding.

**All payments made relative to projects funded under either HOME or FLEX** are made on a reimbursement basis, and only after a careful review of payment requests and supporting documentation. These requests are separate from periodic progress reports, and do not reflect a lack of internal financial control. There is no evidence that any inappropriate payments were made as a result of the review or as a result of delays in receipt of progress related materials.”

*Auditors’ Concluding*

*Comments:*

Although there are no requirements that dictate specific timeframes for monitoring letters and certificates of completion to be issued to the recipients of Small Cities grants, any findings noted as a result of monitoring procedures should be promptly communicated to recipients so that such matters can be resolved in a proper and timely manner and to allow for the proper closeout of projects.

**Inadequate Program Monitoring – Manufacturing Assistance and Urban Act Programs**

*Criteria:*

Assistance agreements between DECD and recipients of Manufacturing Assistance Act (MAA) and Urban Act project funding provide for the following, where applicable:



- Each applicant subject to a federal and/or state single audit must have an audit of its accounts performed annually in accordance with the DECD Audit Guide and the requirements established by federal law and state statute. All applicants not subject to a federal and/or state single audit shall be subject to a project-specific audit of its accounts within 90 days of the completion of the project or at such times as required by DECD. Such audit shall be in accordance with the DECD Audit Guide. At the discretion and with the approval of the commissioner, examiners from DECD may conduct project-specific audits;
- In the event that one of these audits demonstrates that the actual project expenditures made by the applicant are less than the maximum allowable amounts for disbursement by the state, any excess disbursement shall become immediately due and payable to the state by the applicant. Upon repayment by the applicant of such excess amount, the stated amount of the funding under the agreement should be amended to reflect the actual amount of funding received by the applicant;
- Each applicant must provide the commissioner semi-annual project financial statements in the approved DECD project statement format. The information must be provided within 30 days after June 30<sup>th</sup> and December 31<sup>st</sup> until the expiration date of the project financing plan and budget;
- Each applicant must submit quarterly milestone and project reports acceptable to DECD, which delineate progress in the areas of project funding and construction. The reports are due within 30 days of the end of the quarter until the expiration of the project financing plan and budget; and
- Each applicant shall furnish to DECD by the deadline specified in the assistance agreement, a job audit that is performed by a certified public accountant in accordance with the DECD Audit Guide.

The department's Development Manager's Client Service Manual documents various procedures from pre-application to financial closeout, including identifying the information that should be obtained and providing various forms and guidelines for completion. The manual specifies, as applicable, that DECD should receive either the State Single Audit by the statutory date, a State Single Audit Exemption Notification Form indicating the entity's exempt status, or a project-specific audit within 90 days of completion of the project. The manual also outlines the DECD job audit procedures to determine whether the funding recipients'

are in compliance with job creation and retention requirements stipulated in the project assistance agreements.

*Condition:*

A review of MAA and Urban Act project files identified the following deficiencies:

- For three out of four projects tested that required State Single Audits, the department's reviews of the reports were not conducted until ten to 13 months after the reports were received;
- For three out of five projects tested that required project-specific audits, the audits were not completed in a timely manner. For two projects, audits were not completed as of the date of our audit on April 30, 2015, despite being due ten to 13 months earlier. For one project, the audit conducted by DECD was not completed until four years after the audit was required;
- For three out of four projects tested that required semi-annual project financing statements, the recipients submitted the statements up to eight months after they were due. In addition, one of these recipients submitted only one out of four statements that were required;
- For one project tested that required quarterly progress reports, three out of five required reports were submitted late, up to ten months after they were due; and
- For one out of five projects tested that required job audits, the audit was not submitted until four months after the due date specified in the assistance agreement.

*Effect:*

Without receiving required documents and conducting monitoring of projects in a timely manner, the department's ability to review project expenditures and ensure compliance with applicable requirements is impaired. The department may not identify and recover excess disbursements made, nor apply penalties or loan forgiveness credits related to employment obligations in a timely manner.

*Cause:*

Administrative controls over the projects were inadequate. DECD informed us that, due to staffing constraints and task priorities, it could not complete these tasks in a timely manner.

*Recommendation:*

The Department of Economic and Community Development should ensure that a complete review of all projects is performed from the point of application until financial closeout. The department should ensure that assistance agreement requirements and internal control policies are followed. (See Recommendation 13.)

*Agency Response:* “DECD agrees that assistance agreement requirements and internal control policies should be followed. A review of policy and procedures has been conducted to eliminate redundancy, maximize the return from limited staff resources and enhance compliance as follows:

**DECD procedures:** Procedures have been updated to reflect additional steps that improve the timeliness of project close-outs and audits. The additional steps are supportive of DECD sending close-out request forms to companies in a timely fashion and include several reminders to the company to complete the necessary close-out paperwork. This enhanced process will increase DECD’s ability to complete MAA and UA audits in a timely fashion.

**Assistance Agreements for Manufacturing Assistance ACT (MAA):** Three years ago, the department concluded that the requirement for companies to provide annual reports did not provide significant additional value or security and therefore the reporting requirement in assistance agreements was changed to ‘upon the Commissioner’s request.’ This provision allows the team to request for information if needed. The most effective indicator that allows DECD to monitor if a company is still in business is to review the timeliness of loan repayments.

**Urban Act (UA):** After a LEAN process, it was determined that companies, through the close-out process, provided the department with duplicate information. Therefore, effective December 2015, the requirements for companies to provide quarterly reporting was deemed unnecessary and eliminated. Reporting is now required at the end of the project.”

### **Inadequate Compliance Monitoring – Small Business Express Program**

*Criteria:* Assistance agreements between DECD and recipients of Small Business Express program (EXP) funding provide for the following:

- The applicant shall provide a cumulative Statement of Program Cost and Detailed Schedule of Expenditures in the DECD approved format. This information is required to be provided within 90 days after the expiration date of the project financing plan and budget, or earlier as determined by the commissioner; and
- In the event that a required project audit demonstrates that the actual expenditures made by the applicant are less than the maximum allowable amounts for the disbursement by the state, any excess

disbursement made by the state shall become immediately due and payable to the state by the applicant.

DECD Job Audit Procedures outline the processes used to determine the EXP project funding recipients' compliance with job creation and retention requirements stipulated in the assistance agreements, including the required number of jobs to be created and/or retained (employment obligation), the specific 12-month period to be used to determine compliance with the employment obligation, the deadline for completing and submitting a job audit to the state, and whether penalties or credits are applied relative to the attainment of job creation requirements. Once DECD completes a desk review of a job audit, a letter is issued to the funding recipient outlining the results of the job audit and whether any penalty or forgiveness is due. DECD will make adjustments if there are funds to be returned to DECD, loan rate increases due to job shortage penalties, or if loan forgiveness credits are to be applied to loan balances if job goals are met.

*Condition:*

A review of ten EXP project files for which a Statement of Program Cost and Detailed Schedule of Expenditures was due during the audited period identified five applicants that did not provide statements to DECD within the time period specified in the assistance agreements, as follows:

- For three projects, statements were submitted up to six months after they were due; and
- For two projects, statements were not submitted as of the date of our audit on April 30, 2015, five months and 16 months after they were due. Because these statements were not submitted, DECD was not able to verify the actual expenditures made by these recipients.

A review of six job audits completed for EXP projects during the audited period identified the following deficiencies:

- For one project, a job audit was not submitted to DECD until six months after the due date specified in the assistance agreement. Also, the period used by the recipient to demonstrate compliance with the employment obligation was not consistent with the assistance agreement;
- For two projects, DECD did not issue the results of its desk reviews of employment information in a timely manner. For one project, \$2,000 in penalties for the failure to meet employment obligations were not assessed until five months after the desk review was conducted. For the other project, a \$50,000 loan forgiveness credit for employment obligations that were met was not applied to the

outstanding principal balance until six months after the desk review was conducted; and

- For two projects, desk reviews of employment information resulted in loan forgiveness credits of \$50,000 being applied to the outstanding principal loan balances. However, the interest accrual amounts of the loans were not reduced accordingly.

*Effect:* Program requirements and expenditures are not being properly applied and monitored. This has resulted in potential overpayments, penalties, or loan forgiveness credits related to employment obligations not being applied properly or in a timely manner, and overstatements of interest accruals.

*Cause:* Administrative controls over the procurement and review of these reports were inadequate. Errors in interest calculations were the result of clerical errors made during the application of forgiveness credits in the loan management system.

*Recommendation:* The Department of Economic and Community Development should ensure that assistance agreement requirements are adhered to and that specific reports are requested, received, and reviewed within the stipulated timeframes. (See Recommendation 14.)

*Agency Response:* “DECD agrees that the department should ensure that assistance agreement requirements are adhered to and specific reports are requested, received, and reviewed within the stipulated timeframes. DECD notes that the finding is due to a backlog in project close-outs and audits caused by a significant increase in volume of transactions (from 448 required close-outs/audits in 2011 to 722 in 2015) and decreased staffing (from 3.0 FTE to 2.0 FTE). The interview process for an Accounting Career Trainee position was initiated, but is currently on hold due to budget considerations. In lieu of being able to fill the position, the team has developed a plan to work through the backlog using more effective processes and part-time resources.”

### **Unreasonable and Excessive Administrative Fee Terms Included in Agreements with Lending Partners – Small Business Express Program**

*Background:* Section 32-7g of the General Statutes established the Small Business Express program (EXP) within DECD to provide Connecticut-based small businesses with various forms of financial assistance, including revolving loans to support growth, deferrable or forgivable job creation incentive loans, and matching grants. Assistance amounts may range from \$10,000 to \$100,000 for grants and revolving loans, and up to \$300,000 for

deferrable or forgivable loans. Loans can carry a maximum repayment rate of four percent and can be for a term of up to ten years. DECD may partner with lenders of the Connecticut Credit Consortium (lending partners), established under Section 32-9yy of the General Statutes, to fulfill the requirements of the program.

Effective in April 2012, DECD entered into lending agreements with six lending partners to administer, service, and monitor the financial assistance provided under the program and to provide on-going technical assistance. From the program's inception through June 30, 2015, the lending partners provided assistance totaling over \$31 million to 244 recipients.

In accordance with the terms of the agreements, DECD would provide the lending partners annual technical assistance services fees of \$3,500 (\$1,750 paid semiannually) for each borrower that was provided such services and annual servicing fees equal to three percent (1.5 percent paid semiannually) of the outstanding principal balance of all loan portfolios. Also, 50 percent of the interest received on loan portfolios during the calendar year could be retained by the lending partners.

*Criteria:* Section 32-7h of the General Statutes allows DECD to provide for the payment of administrative expenses incurred by DECD or its lending partners in carrying out EXP not to exceed four percent of program funding.

*Condition:* From the program's inception through June 30, 2015, the State Bond Commission approved a total of \$200 million in EXP funding, thereby allowing for up to \$8 million in administrative expenses to be incurred under the program. During this period alone, total administrative fees paid to the lending partners amounted to over \$4.5 million, or 57 percent of the amount allowed. If administrative fees continued to be paid under the terms of the existing agreements, based on the department's projections, over \$15 million in administrative fees would be paid through June 30, 2024, not including retained interest of \$2.3 million. In addition, the lending agreement terms, particularly related to smaller loan amounts, would result in administrative fees being paid to the lending partners over the terms of the loans that exceed the actual loan amounts.

Following DECD management's realization that administrative fees were excessive, in order to reduce the fees and to ensure adherence to the statutory limit, DECD offered to provide each lending partner with \$1 million in new program funding if the partner accepted amendments to the terms of the original agreement and a new agreement for the additional funding. Pursuant to Section 4.1 of the agreements, effective June 30, 2015, DECD terminated agreements with two lending partners

that did not agree to the proposed modifications. A significant decrease was noted in the amount of administrative fees paid to the lending partners as a result of the amended agreements.

*Effect:* Unreasonable and excessive administrative fees were being paid to the lending partners under the terms of the original lending agreements.

*Cause:* The original lending agreements were executed without adequate analysis of the potential administrative expenses payable to the lending partners or consideration of the statutory limitation.

*Recommendation:* The Department of Economic and Community Development should ensure more careful analysis and consideration of any statutory limitations and other applicable requirements when executing assistance agreements to avoid any similar issues in the future. (See Recommendation 15.)

*Agency Response:* “The department recognized this issue and took appropriate action. To reduce excessive administrative fees and ensure adherence to the statutory limit of four percent of program funding, DECD amended the terms of the original lending partner agreements with four of the six lending partners. Agreements were terminated with the other two lending partners.

The amendments, effective July 1, 2015, made the following changes which resulted in decreased fees being paid:

1. Technical assistance fees will no longer be allowed.
2. DECD will provide an annual servicing fee equal to one and one half (1.5) percent of the outstanding principal loan balance. This is a reduction from three (3) percent.
3. All interest received on loans will now be returned to DECD.

To avoid similar issues in the future, DECD will perform financial analysis with careful consideration of the impact and statutory limitations related to partner agreements.”

## **Service Organization Controls Reports**

*Background:* Section 32-7g of the General Statutes established the Small Business Express program (EXP) within DECD to provide Connecticut-based small businesses with various forms of financial assistance, including revolving loans to support growth, deferrable or forgivable job creation incentive loans, and matching grants. Assistance amounts may range from \$10,000 to \$100,000 for grants and revolving loans, and up to \$300,000 for

deferrable or forgivable loans. Loans can carry a maximum repayment rate of four percent and can be for a term of not more than 10 years. DECD may partner with lenders of the Connecticut Credit Consortium (lending partners), established under Section 32-9yy of the General Statutes, to fulfill the requirements of the program.

DECD entered into lending agreements with a total of six lending partners to administer, service, and monitor the various forms of financial assistance provided under the program and to provide on-going technical assistance to borrowers. The six lending partners combined administer 244 loans and grants amounting to over \$31 million.

In accordance with Section 32-7h of the General Statutes, up to four percent of EXP funding can be used for the payment of administrative expenses incurred by DECD or its lending partners in carrying out the program. Since administrative expenses were initially paid to the lending partners from June 2012 through the period ended June 30, 2015, a total of over \$4.5 million in combined administrative expenses were paid. Furthermore, as of January 1, 2016, bond commission approvals for the program totaled \$222 million, thus allowing for up to \$8.9 million in administrative expenses.

*Criteria:* Entities reporting loan receivables administered by third-party loan servicers should ensure that reported amounts reflect loan receivable balances carried by the loan servicers.

Management is responsible for implementing and maintaining effective internal controls over financial reporting. Sound internal controls of a user entity provide for the receipt of a Service Organization Controls 1 (SOC 1) Report, prepared in accordance with Statement on Standards for Attestation Engagements No. 16 (SSAE 16), issued by the American Institute of Certified Public Accountants to ensure the effectiveness of internal controls at service organizations that maintain significant financial applications and processes.

*Condition:* DECD (the user entity) has not ensured that the lending partners (the service organizations) responsible for administering financial assistance provided under EXP have had SOC 1 Reports performed on their financial applications and processes.

*Effect:* Without SOC 1 Reports, DECD cannot fully monitor and assess the design and operating effectiveness of the controls in place over the financial assistance being administered by the lending partners. Furthermore, the loans being administered may not be properly accounted for or reported and, as a result, financial disclosures on the state's financial statements may be inaccurate.



*Cause:* Lending agreements in place between DECD and the lending partners do not require SOC 1 Reports, and DECD management may not have considered the importance and relevance of these reports.

*Recommendation:* The Department of Economic and Community Development should consider requiring its lending partners, which are responsible for administering and servicing financial assistance provided under the Small Business Express program, to obtain a Service Organization Controls (SOC 1) Report prepared in accordance with Statement on Standards for Attestation Engagements No. 16 (SSAE 16). (See Recommendation 16.)

*Agency Response:* “DECD considered the recommendation that we require a Service Organization Controls (SOC 1) Report prepared in accordance with Statement on Standards for Attestation Engagements No. 16 (SSAE 16) from lending partners. This report is not required by statute or regulation. DECD has decided not to require this report because of the burdensome cost it would create on our lending partners. DECD oversees the work of lending partners and reviews performance as appropriate to ensure the effective use of resources.”

*Auditors’ Concluding  
Comments:*

In consideration of the amount of the loans administered and the potential impact that incorrect accounting or reporting could have on the state’s financial statements, it would appear that the financial burden to the lending partners would be nominal in relation to the administrative fees received. Therefore, the Auditors of Public Accounts maintains that DECD should more carefully consider the usefulness of the SOC 1 Report for ensuring both the effectiveness of the lending partners’ internal controls and the accuracy of the state’s financial statements.

**Documentation Supporting Altered Information to DECD Records**

*Criteria:* An adequate system of internal control requires that any altered information to already approved documents be supported by documentation authorizing such altered information.

DECD uses a Project Financing Plan & Budget form to document the approved project budget period, project funding, specific costs, and any revisions.

*Condition:* Our review of Project Financing Plan & Budget forms pertaining to one project disclosed an instance in which the start date of the budget period under the Budget Period Approved by DECD section of the form was altered; it was changed from 12/7/2012 to 8/1/11 with no indication as to who changed it or when it was changed. This change allowed expenses

to be charged to the project prior to December 7, 2012, the project start date under the approved assistance agreement. Section 3.2.G. of the approved assistance agreement states that, “Unless authorized by the Commissioner in writing, no costs incurred prior to December 7, 2012, are eligible for payment from the Funding.” In response to our inquiry regarding the commissioner’s written authorization, DECD indicated that the Project Financing Plan & Budget form was the commissioner’s written authorization allowing costs incurred prior to December 7, 2012, and provided an explanation supporting its response. The after-the-fact explanation provided by DECD for allowing pre-agreement costs to be charged to the project may be valid, but is not an acceptable way of documenting significant changes made to existing agreements.

*Effect:* Undocumented changes to already approved project requirements increase the risk of unauthorized transactions being executed.

*Cause:* We did not determine the cause.

*Recommendation:* The Department of Economic and Community Development should require that any changes to approved contract terms be supported by adequate documentation authorizing such changes. (See Recommendation 17.)

*Agency Response:* “DECD agrees with the finding, with the following clarification.

It is standard agency practice that the initial Bond Commission approval date is the project start date. Initial costs, not covered by DECD funding, were incurred prior to the start date and pertained to the overall scope of this Brownfield/redevelopment project. After reviewing the documentation, DECD deemed these costs as eligible, non-DECD contributions to the project. Section 3.2.G. of the assistance agreement (Pre-agreement Costs) states that “Unless authorized by the Commissioner in writing, no costs incurred prior to December 7, 2012, are eligible for payment from the Funding.” Approval by the Commissioner was obtained and documented. DECD did not approve disbursement of, or issue payment for, any state funds to reimburse costs incurred before the project start date.

Since DECD was in compliance with the assistance agreement, it was not necessary to change the project start date. The date was whited out in error. The following steps will be taken to ensure that no undocumented changes are made to previously approved project documents for consideration of expenses which were incurred prior to the project start date:

- Per Section 3.2.G of the assistance agreement, we will require all of our funding recipients who request consideration of costs incurred prior to the project start date, to submit a letter requesting approval by the DECD Commissioner.
- DECD will review the request to determine if costs can be deemed eligible for DECD funding and allow them to be covered under the funding program before the project start date.
- DECD will then issue a letter to the funding recipient either approving or denying the request.
- The Project Start Date will never be modified in our Project Financing Plan & Budget without amending the assistance agreement.”

### **Review of Boards, Councils, Committees, and Commissions**

*Background:* The General Statutes relating to DECD provide for various boards, councils, committees, and commissions, which will be collectively referred to as boards and include the State Historic Preservation Board, Culture and Tourism Advisory Committee, Connecticut Arts Council, Historic Preservation Council, Sports Advisory Board, Small Business Advisory Board, and the Commission on Connecticut’s Future.

*Criteria:* Section 1-225 of the General Statutes requires that meeting minutes of a public agency be made available for public inspection and posted to the public agency’s website no later than seven days after such meeting, that the schedule of regular meetings of the public agency for the ensuing year be filed with the Secretary of the State no later than January 31<sup>st</sup> of each year and posted on the public agency’s website, and that the agenda of regular meetings be filed with the Secretary of the State no less than 24 hours before each meeting and posted to the public agency’s website.

Section 10-408a of the General Statutes provides that any member of the Connecticut Arts Council who fails to attend three consecutive meetings or who fails to attend 50 percent of all meetings held during a calendar year shall be deemed to have resigned.

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

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

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

*Condition:* Our review of the boards for fiscal years ended June 30, 2013 and 2014, and through the date of our review in November 2015, disclosed the following:

- Approved meeting minutes of the State Historic Preservation Board, Connecticut Arts Council, and Historic Preservation Council were not posted to the DECD website within seven days of the respective meeting being held, and a schedule of meetings of the Connecticut Arts Council for the 2015 calendar year was not filed with the Secretary of the State by the January 31<sup>st</sup> deadline.
- A review of board meeting attendance disclosed that a total of seven members of the Connecticut Arts Council and the Historic Preservation Council missed three consecutive meetings and/or failed to attend fifty percent of all the meetings held in a calendar year. Despite being deemed to have resigned, these board members continued to serve.
- DECD informed us that the Commission on Connecticut's Future and the Small Business Advisory Board have not been active and there were no attempts to rescind the statutes to remove these boards.

*Effect:* The boards were not always operating in compliance with the General Statutes regarding freedom of information laws and other legal requirements. Members of the public were not able to examine records of the activity of these boards. The composition of these boards is not as intended if members fail to attend meetings.

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

*Recommendation:* The Department of Economic and Community Development should work with the boards to ensure compliance with Freedom of Information Act requirements and applicable General Statutes, and should notify appointing authorities of any attendance issues to ensure adequate

representation at all board meetings. Also, the department should either pursue the repeal of the statutory mandate or reconstitute the Commission on Connecticut's Future and the Small Business Advisory Board in accordance with Sections 32-245 and 32-9xx of the General Statutes, respectively. (See Recommendation 18.)

*Agency Response:* "DECD acknowledges the finding with the following clarifications.

**Board Member Attendance:** Board members are Gubernatorial and legislatively appointed and serve as volunteers. If five out of ten board members miss three consecutive or 50 percent of meetings during a calendar year and are deemed resigned, items that require motions and votes would need to be tabled and no business could be conducted due to the lack of a quorum. Grants, contracts, and specific allocation for funds are examples of items for which quorums are necessary.

DECD will work with the board chairs of the Historic Preservation Council and the Arts Council to comply with the attendance protocol by sending additional reminders to board members quoting the statutes regarding their participation requirement prior to each meeting.

**Minutes:** The Historic Preservation Council and other board meetings are technical in nature and two to three hours in duration. Lack of administrative staff has made responding in a timely fashion challenging.

DECD will reallocate staff responsibilities to meet this requirement.

**Commission on Connecticut's Future and the Small Business Advisory Board:** DECD has engaged with the Governor's office and other elected officials about eliminating some of these defunct and unnecessary committees and reports. DECD will continue working with the Governor and Legislators as legislative priorities allow."

## RECOMMENDATIONS

Our prior audit report on the Department of Economic and Community Development contained 15 recommendations for improving operations, 12 of which were repeated or restated with modifications in the current audit report. Our current audit report presents 18 recommendations, including six new recommendations.

*Status of Prior Audit Recommendations:*

- **DECD should improve its cash management procedures by only disbursing funds for immediate needs and reducing the time to receive refunds of overpayments.** Rewording assistance agreements should be considered to require earlier refunds. This recommendation was not implemented and is being repeated. (See Recommendation 1.)
- **DECD should implement formal policies and procedures to ensure that unused balances from prior State Bond Commission approvals are identified in a timely manner and returned to the unallotted balance under the fund once a project is completed or cancelled.** This recommendation was not fully implemented and is being repeated. (See Recommendation 2.)
- **DECD should perform complete reconciliations of receivable activity and balances before reporting balances to the State Comptroller. For Energy Conservation Loan balances, DECD should attempt to reconcile the differences between the loan servicer and DECD amounts. DECD should require a report prepared pursuant to Statement on Standards for Attestation Engagements No. 16.** This recommendation was not implemented and is being repeated. (See Recommendation 3.)
- **DECD should ensure that all managers are evaluated on an annual basis through the use of PARS evaluation forms.** This recommendation was implemented and is not being repeated.
- **DECD should reconcile total payroll costs allocated by its Time Processing System to total payroll costs reflected in appropriation expenditure accounts in Core-CT's general ledger. Payroll costs allocated by the Time Processing System should ultimately be recorded in the general ledger appropriation accounts, or alternately if not recorded, be sufficiently documented by DECD explaining the reason(s) why the costs were not recorded.** This recommendation was implemented and is not being repeated.
- **DECD should ensure that overtime earned is properly approved within the timeframe that is required.** This recommendation was not implemented and is being restated for conditions related to approvals of compensatory time. (See Recommendation 5.)

- **DECD should ensure that all out-of-state travel is properly documented, authorized, and reported.** This recommendation was implemented in part and is being repeated for current conditions noted. (See Recommendation 7.)
- **DECD should strengthen its internal controls to ensure that funds are committed prior to purchasing goods and services, and receipt dates are recorded accurately.** This recommendation was implemented in part and is being restated for current conditions noted. (See Recommendation 8.)
- **DECD management should test its Information Technology Disaster Recovery Plan and properly coordinate all contingency provisions with the plan.** This recommendation was implemented in part and is being restated for current conditions noted. (See Recommendation 9.)
- **DECD should meet the reporting deadline and requirements when submitting the Asset Management/Inventory/GAAP Reporting Form CO-59.** This recommendation was not implemented and is being restated for current conditions noted. (See Recommendation 10.)
- **DECD should ensure all offices maintain and control their assets with detailed records, including tag numbers, and should perform complete annual physical inspections.** This recommendation was not implemented and is being restated for current conditions noted. (See Recommendation 11.)
- **DECD should ensure that assistance agreement requirements as well as internal controls and records retention policies are followed.** This recommendation was not implemented and is being repeated. (See Recommendation 12.)
- **DECD should ensure that a complete review of all projects is performed from the point of application until final closeout. The department should retain all supporting documentation used to evaluate the applicant's eligibility for financial assistance in accordance with the State Library's records retention requirements.** This recommendation was not implemented and is being restated for current conditions noted. (See Recommendation 13.)
- **DECD should ensure that assistance agreement requirements are adhered to and specific reports are requested, received, and reviewed within stipulated timeframes.** This recommendation was not implemented and is being repeated. (See Recommendation 14.)
- **DECD should seek legislative clarification regarding the department's ability to impose requirements and restrictions on the funding of certain budgetary line items. Consideration should be made to enact legislation detailing stated requirements on directed legislative funds or line item amounts given to recipients within the budget.** The department implemented procedures related to the monitoring of directed local funds and this recommendation is not being repeated.

*Current Audit Recommendations:*

- 1. The Department of Economic and Community Development should improve its cash management procedures by only disbursing funds for immediate needs and reducing the time to collect refunds of overpayments. Rewording of assistance agreements should be considered to require more timely refunds.**

Comment:

During the fiscal year ended June 30, 2013, DECD issued 166 Certificates of Approved Program Cost and State Funding that reflected amounts due to DECD totaling \$685,625. The length of time that grantees held unexpended state funds appeared to be excessive.

- 2. The Department of Economic and Community Development should fully implement formal policies and procedures to ensure that unused balances from prior State Bond Commission approvals are identified in a timely manner and returned to the unallotted balance under the fund once a project is completed or cancelled.**

Comment:

During prior audits, we found that DECD had not developed formal policies and procedures to address the administration of unexpended balances on bond-financed projects. Our current review noted that policies and procedures had been approved, but were only partially implemented beginning in March 2015.

- 3. The Department of Economic and Community Development should perform complete reconciliations of receivable activity and balances before reporting balances to the State Comptroller.**

**For Energy Conservation Loan balances, DECD should attempt to reconcile the differences between the loan servicer and DECD amounts. DECD should require a report prepared pursuant to Statement on Standards for Attestation Engagements No. 16.**

Comment:

Grant Refunds:

Reconciliations of grant refund activity and reported receivable balances were not performed.

ECL Loans:

The department's reconciliations of ECL principal balances in its records to amounts reported monthly by the loan servicer include unresolved items. Furthermore, DECD did not require that the ECL loan servicer provide a report on its controls pursuant to SSAE 16.



- 4. The Department of Economic and Community Development should ensure the proper calculation of loan interest receivables and consistency with the amounts billed to recipients in accordance with financial assistance agreements.**

Comment:

Our review of loan interest receivables for the fiscal years ended June 30, 2013 and 2014 noted that interest accruals in the department's loan management system do not always agree with the amounts billed to recipients and the terms of assistance agreements. Furthermore, interest receivable amounts reported to the State Comptroller were not accurate.

- 5. The Department of Economic and Community Development should ensure that overtime and compensatory time is properly approved within the required timeframe.**

Comment:

Our review of overtime and compensatory time during the audited period disclosed instances in which employees were paid overtime or earned compensatory time without proper prior authorization.

- 6. The Department of Economic and Community Development should ensure the correct recording and accrual of state service time eligible towards longevity to ensure that longevity payments are made in accordance with state statutes and collective bargaining agreements.**

Comment:

Our review of longevity payments disclosed that two employees received longevity payments that they were not entitled to.

- 7. The Department of Economic and Community Development should ensure that all out-of-state travel is properly documented, authorized, and reported.**

Comment:

Our review of the department's documentation related to out-of-state travel during the period beginning July 1, 2013 through June 30, 2014 revealed that eight trips were not reported to the Office of Policy and Management in accordance with the Governor's directive.

- 8. The Department of Economic and Community Development should strengthen its internal controls to ensure that funds are committed prior to purchasing goods and services.**

Comment:

Through our review of expenditures, we noted that 47 purchase orders were created and/or approved after the receipt of goods or services and three expenditures were made without the issuance of a purchase order.

- 9. The Department of Economic and Community Development should continue its efforts to develop a current comprehensive information technology disaster recovery plan, including the proper coordination and periodic testing of contingency provisions within the plan.**

Comment:

The department did not have a current comprehensive information technology disaster recovery plan in place or provisions for a backup site, computer hardware and software.

- 10. The Department of Economic and Community Development should improve internal controls over asset accountability and reporting to ensure compliance with the requirements of the State Property Control Manual.**

Comment:

The CO-59 form for the fiscal year ended June 30, 2013 was submitted seven months late.

The museums' reportable collection items were not reported accurately on the CO-59 form.

Only one of the four museum's gift shop inventories was reported on the CO-59 form for the fiscal year ended June 30, 2013. Although all of the museums' inventories were reported for the fiscal year ended June 30, 2014, the ending balance was understated by \$7,427. Furthermore, addition or deletion amounts on the CO-59 form for both fiscal years were not supported.

- 11. The Department of Economic and Community Development should ensure the proper maintenance and control of its assets with detailed records, including tag numbers. Furthermore, the department should continuously survey its inventory levels and perform complete annual physical inspections.**

Comment:

Our review of assets identified one item that could not be located, six that were found in locations other than indicated in Core-CT, and one that we physically inspected although it was listed as disposed in Core-CT. Also, numerous assets had both DECD and CCT tags attached and there were inconsistencies as to which tag was used for recording purposes. In addition, numerous items seemed no longer required for use, yet no steps had been taken by the department to dispose of them.

A review of disposed assets disclosed four items that were not properly deleted from Core-CT and were observed during a physical inspection.

Not all of the department's assets were physically inspected during fiscal year 2013-2014, and there were no physical inspections conducted of the four museums' collection items.

The museums' collection items do not appear to contain the minimum data required for a property control record and not every collection item is recorded in the system.

**12. The Department of Economic and Community Development should ensure that assistance agreement requirements and internal control policies are followed.**

Comment:

Our review of five Small Cities, five HOME, and five FLEX projects identified eligibility review forms, quarterly progress reports, semi-annual project financing statements, and cost certifications that were either missing or not submitted to DECD in a timely manner. In addition, we noted instances of the untimely performance of project monitoring and issuance of monitoring results by DECD.

**13. The Department of Economic and Community Development should ensure that a complete review of all projects is performed from the point of application until financial closeout. The department should ensure that assistance agreement requirements and internal control policies are followed.**

Comment:

Our review of Manufacturing Assistance and Urban Act projects noted semi-annual project financing statements and progress reports that were not submitted to DECD in a timely manner or were not submitted at all; job audits and project-specific audits that were not completed by due dates stipulated in assistance agreements; and reviews of audit reports that were not conducted by DECD in a timely manner.

**14. The Department of Economic and Community Development should ensure that assistance agreement requirements are adhered to and that specific reports are requested, received, and reviewed within the stipulated timeframes.**

Comment:

A review of ten Small Business Express program (EXP) project files identified five applicants that did not provide a completed Statement of Program Cost and Detailed Schedule of Expenditures within the time period specified in the assistance agreements.

A review of six job audits completed for EXP projects identified one project for which a job audit was submitted late and was based on a period that was inconsistent with the assistance agreement; two projects for which DECD did not issue results of its desk

reviews in a timely manner; and two projects for which DECD desk reviews resulted in loan forgiveness credits being applied without reducing interest accrual amounts accordingly.

- 15. The Department of Economic and Community Development should ensure more careful analysis and consideration of any statutory limitations and other applicable requirements when executing assistance agreements to avoid any similar issues in the future.**

Comment:

Since the inception of the Small Business Express program (EXP) in April 2012 and through June 30, 2015, total administrative fees paid to the lending partners under the program amounted to over \$4.5 million, or 57 percent of the \$8 million statutorily allowed. If administrative fees continued to be paid under the terms of the original agreements, over \$15 million would be paid through June 30, 2024, not including retained interest of \$2.3 million. In addition, the lending agreement terms, particularly related to smaller loan amounts, would result in administrative fees being paid to the lending partners over the terms of the loans that exceed the actual loan amounts.

- 16. The Department of Economic and Community Development should consider requiring its lending partners, which are responsible for administering and servicing financial assistance provided under the Small Business Express program, to obtain a Service Organization Controls (SOC 1) Report prepared in accordance with Statement on Standards for Attestation Engagements No. 16 (SSAE 16).**

Comment:

DECD has not ensured that the lending partners responsible for administering financial assistance provided under the Small Business Express program have had Service Organization Controls (SOC 1) Reports performed on their financial applications and processes.

- 17. The Department of Economic and Community Development should require that any changes to approved contract terms be supported by adequate documentation authorizing such changes.**

Comment:

Our review of a project disclosed that the start date of the budget period for the project was altered on the related Project Financial Plan and Budget form with no indication as to who changed it or when it was changed. This change allowed expenses to be charged to the project prior to the project start date under the approved assistance agreement. This is not an acceptable way of documenting significant changes to existing approved agreements.

- 18. The Department of Economic and Community Development should work with the boards to ensure compliance with Freedom of Information Act requirements and applicable General Statutes, and should notify appointing authorities of any attendance issues to ensure adequate representation at all board meetings. Also, the department should either pursue the repeal of the statutory mandate or reconstitute the Commission on Connecticut's Future and the Small Business Advisory Board in accordance with Sections 32-245 and 32-9xx of the General Statutes, respectively.**

Comment:

Our review of the department's various boards disclosed noncompliance with the general statutes regarding Freedom of Information laws and other statutory requirements. In addition, we were informed of two boards that have not been active, and there were no attempts to rescind the statutes to remove these boards.

**CONCLUSION**

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

*Vincent Filippa*

Vincent Filippa  
Principal Auditor

Approved:



John C. Geragosian  
Auditor of Public Accounts