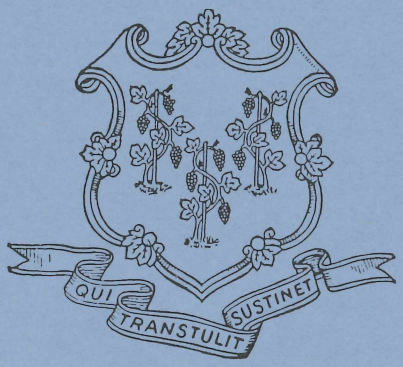
CRRA AND OTHER QUASI-PUBLIC AGENCIES

Connecticut

General Assembly



LEGISLATIVE
PROGRAM REVIEW
AND
INVESTIGATIONS
COMMITTEE

December 2002

CONNECTICUT GENERAL ASSEMBLY
LEGISLATIVE PROGRAM REVIEW AND INVESTIGATIONS COMMITTEE

The Legislative Program Review and Investigations Committee is a joint, bipartisan, statutory committee of the Connecticut General Assembly. It was established in 1972 to evaluate the efficiency, effectiveness, and statutory compliance of selected state agencies and programs, recommending remedies where needed. In 1975, the General Assembly expanded the committee's function to include investigations, and during the 1977 session added responsibility for "sunset" (automatic program termination) performance reviews. The committee was given authority to raise and report bills in 1985.

The program review committee is composed of 12 members. The president pro tempore of the Senate, the Senate minority leader, the speaker of the house, and the House minority leader each appoint three members.

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LEGISLATIVE PROGRAM REVIEW
& INVESTIGATIONS COMMITTEE

CRRA and Other Quasi-Public Agencies

DECEMBER 2002

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CRRA AND OTHER QUASI-PUBLIC AGENCIES

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DIGEST
CRRA and Other Quasi-Public Agencies

Background

- *A Quasi-public agency (QPA) is an entity created by law as a government corporation with the power to raise and expend funds outside the government's administrative and financial controls.*
- *The Connecticut Resources Recovery Authority (CRRA) was established as a QPA in 1973, to develop and implement solid waste disposal, recovery, and recycling facilities.*
- *CRRA oversees four comprehensive solid waste disposal projects including: Mid-Connecticut, Wallingford, Bridgeport, and Southeast. Each project has its own unique legal, financial, contractual, and operational structure.*
- *In FY 02, CRRA had operating revenues of $157.5 million and expenses of $173.0 million. Service fees accounted for 66 percent of the revenues. Earning from the generation of electricity contributed 27 percent of the revenues.*
- *The principal on CRRA bonds outstanding as of June 30, 2002, was $239.0 million, of which $204.6 was backed by the state.*

Problems

- *A failed deal with Enron led to an estimated $24 million decrease in operating revenues for CRRA's Mid-Connecticut project in FY 02.*
- *CRRA lacked the administrative controls and oversight mechanisms necessary to assure compliance with the authority's own policies and procedures.*
- *CRRA operated under a management culture that ignored legislative policies and mandates and pursued its own interests in a somewhat ad hoc manner.*

Response to Problems

- *An act passed during the 2002 legislative session replaced CRRA's old board of directors with a new one effective June 1, 2002*
- *The new board has taken a number of steps to deal with CRRA's problems. It adopted a mission statement that emphasizes the importance of municipalities, rewrote the authority's policies and procedures to assure more accountability, worked closely with the attorney general in pursuit of money lost in the Enron deal, and selected a new president.*

Alternative models

- *Models for managing solid waste disposal systems include: public agency, quasi-public agency, and private industry.*
- *While the most popular approach appears to be the QPA model, examples of all three have been found in operation.*

- *None of the models considered for handling the disposal of municipal solid waste were clearly superior under all applicable criteria.*

Changing models

- *Changing the state's management model for solid waste disposal from a quasi-public agency to either a state agency or private sector model prior to 2015 would have to be done on a project-by-project basis and require renegotiating existing agreements with municipalities, vendors, and bondholders.*

RECOMMENDATION

CRRA should be continued as a quasi-public agency through at least 2008.

At least three full years prior to the scheduled termination of the municipal service agreements governing a project, the CRRA board should form a special committee consisting of representatives of the authority and all municipalities involved in the project to develop options for disposing of solid waste at the conclusion of the existing agreement.

The options analyzed by each special committee should include turning the function over to the private sector.

Other quasi-public agencies

- *The reimbursement policies now in effect at quasi-public agencies governing the personal use of vehicles, cell phones, and credit cards, preclude the need for legislative action.*
- *The state's quasi-public agencies are not in compliance with the spirit of C.G.S Section 1-122, or in selected instances the requirements of C.G.S. Section 1-123, governing the reporting of information to the General Assembly and the public.*
- *Noncompliance with reporting requirements by quasi-public agencies is made possible by the General Assembly's lack of a formal system to track and assess reports required of quasi-public agencies.*
- *Critical data on the financial activities and operational practices of quasi-public agencies are not developed by sources independent of the agencies.*

RECOMMENDATIONS

The board of directors of each quasi-public agency identified in C.G.S. Section 1-120, if it has not already done so, should adopt written policies governing the use of vehicles, cell phones, credit cards, and such other items as the board deems necessary.

Reports required by C.G.S. Section 1-122 and Section 1-123 should be submitted to the Legislative Program Review and Investigations Committee for an assessment as to whether the reports meet the statutory requirements. Within 30 days of receiving

a report, the program review committee should notify those designated to receive the report of its availability and the committee's assessment of the report's compliance with legislative intent.

The State Auditors of Public Accounts shall be responsible for performing or contracting for the performance of all compliance and financial audits of the quasi-public agencies identified in C.G.S. Section 1-120. Each quasi-public agency shall annually pay the state auditors for the cost of the audits, whether performed by in-house audit staff or through a contract with an outside audit firm.

Introduction

Purpose of the study

The objective of this study was to determine whether the Connecticut Resources Recovery Authority (CRRA) should be operated as a quasi-public agency (QPA), state agency, or eliminated with its role being assumed by the private sector. A secondary focus was to ascertain the extent to which the practices of the state's other quasi-public agencies raise concerns requiring legislative attention.

Methodology

The committee through its staff interviewed CRRA staff and reviewed the legislative record surrounding the creation of the authority. Committee staff also observed meetings of CRRA's new board of directors and toured its facilities. Data on the state's other quasi-public agencies were obtained from their annual reports and responses to a survey mailed to each QPA.

The committee's 1988 report on the state's quasi-public agencies provided a framework for the study. This was supplemented by an extensive review of the national literature on resource recovery facilities and quasi-public agencies.

A briefing report on CRRA was given to the committee by its staff on October 8, 2002. A public hearing was held November 14, 2002. The committee adopted the findings and recommendations contained in this report December 18, 2002.

Chapter One

Quasi-Public Agencies - Characteristics

Definition

For the purposes of this study, a quasi-public agency is an entity created by state statute as a government corporation:

- answering to an independent governing board appointed by state officials;
- providing a specific public benefit;
- generating and expending funds outside of the state's budgetary process; and
- operating independent of most state government administrative and financial controls.

Rationale

An entity is created as a quasi-public agency based on a belief the state's requirements and controls would prevent a rapid response to changes in the conditions and demands under which the entity must operate.

Controls imposed on state agencies

- Budget process
- Bonding process
- Personnel system
- Property acquisition process
- Contracting for technical and personal services
- Affirmative action plan and implementation
- Uniform Administrative Procedure Act
- Code of Ethics
- Freedom of Information
- Auditors of Public Accounts

The General Assembly in creating or reshaping quasi-public agencies has applied these controls selectively. In instances where the controls do not apply, each QPA's board is required to develop its own procedures, or in some cases, such as issuing bonds, an agency must follow special requirements included in its enabling statute.

Table I-1 shows the current application of the controls to specific quasi-public agencies.

Table I-1. Applicability of State Government Controls to Quasi-Public Authorities

Control	*CDA*	*CII*	*CHEFA*	*CHESLA*	*CHFA*	*SHA (2)*	*CRRA*	*CHWMS*	*CPA*	*CCEDA*	*CLC*
Budget	No	No	No	No	No	No	No	No	(3)	No	No
Bonding	No (1)	Yes	No	No	No	Yes	No	Yes	Yes	Yes	Yes
Personnel	No	No	No	No	No	No	No	No	(3)	No	No
Purchasing	No	No	No	No	No	No	No	No	No	No	No
Contracting	No	No	No	No	No	No	No	No	No	No	No
Affirmative Action	No	No	No	No	No	No	No	No	No	No	No
UAPA	No	No	No	No	No	No	No	No	No	No	No
Code of Ethics	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
FOI	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
State auditors	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

UAPA = Uniform Administrative Procedure Act
FOI = Freedom of Information
CDA = CT Development Authority
CII = CT Innovations Incorporated
CHEFA = CT Health and Educational Facilities Authority
CHESLA = CT Higher Education Supplemental Loan Authority
CHFA = CT Housing Finance Authority
SHA = CT Housing Authority
CRRA = CT Resources Recovery Authority
CHWMS = CT Hazardous Waste Management Service
CCPA = CT Port Authority
CCEDA = Capital City Economic Development Authority
CLC = CT Lottery Corporation

(1) Under insurance mortgage program the State Bond Commission issues bonds, the proceeds of which are funneled through the Department of Economic and Community Development to CDA.

(2) The State Housing Authority is a subsidiary of CHFA.

(3) Currently the Department of Transportation provides staff to CPA, and its activities are funded through the Special Transportation Fund.

Chapter Two

CRRA Overview

The Connecticut Resources Recovery Authority was established in 1973 as a quasi-public agency (P.A. 73-459).

The purpose of the authority is to develop and implement solid waste recycling, disposal, and recovery systems and facilities designed to serve municipalities, regions, and private entities.

To meet this purpose CRRA has been given the power to:

- employ staff;
- acquire property;
- enter into contracts to develop, operate, or manage facilities and systems; and
- issue bonds.

CRRA oversees the operation of four resources recovery facilities, three recycling facilities, six landfills, and 12 transfer stations.

The authority is comprised of four comprehensive solid waste disposal projects, a non-project ventures group, and an administrative pool. The projects are centered on the resources recovery facilities located in Bridgeport, Hartford (Mid-Connecticut), Wallingford, and Preston (Southeast). Vendors operate the facilities and provide services under agreements with CRRA. Each project has a unique legal, contractual, financial, and operational structure.

Table II-1. Selected Information by Project

Project	*Towns Served*	*Tons of Waste Disposed (a)*	*Fees Charged Per Ton (b)*	*Main Facility Operator*
Mid-Connecticut	70	880,000	$57	Metropolitan District Commission
Bridgeport	18	880,000	$69	Wheelabrator
Wallingford	5	153,300	$55	Covanta Energy
Southeast	13	195,000	$57	American Ref-Fuel

(a) Year ended June 30, 2001
(b) Fee for FY 03
Source of Data: Various CRRA reports

Board of Directors

CRRA's powers are vested in a 13-member board of directors. The governor appoints three members, the legislative leaders appoint eight, and there are two ex-officio members -- the secretary of the Office of Policy and Management (OPM) and the state treasurer.[1]

Five of the 13 board members must be municipal officials, four must have extensive high level experience in corporate finance, business or industry, one must have extensive high level experience in the energy field, and one must have extensive high level experience in the environment field.

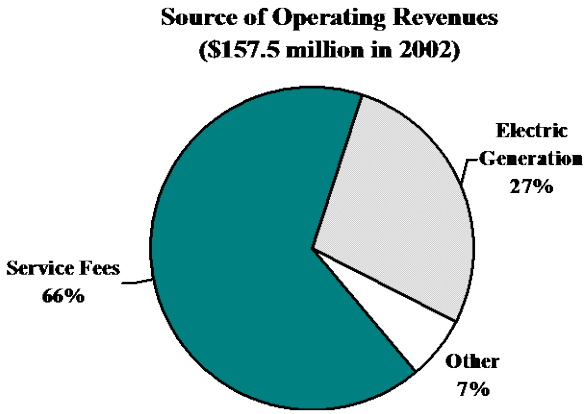
The governor, with the advice and consent of both houses of the General Assembly, designates one of the directors to serve as chairperson of the board.

The board has the power to act by a majority of the directors present during any meeting at which a quorum -- seven directors including at least two directors from municipal government and either the secretary of OPM or the state treasurer -- is in attendance.

Finances

The authority is required by statute to be self-sustaining. Its income is derived primarily from fees for the services it provides to municipalities and private entities and the sale of electricity.

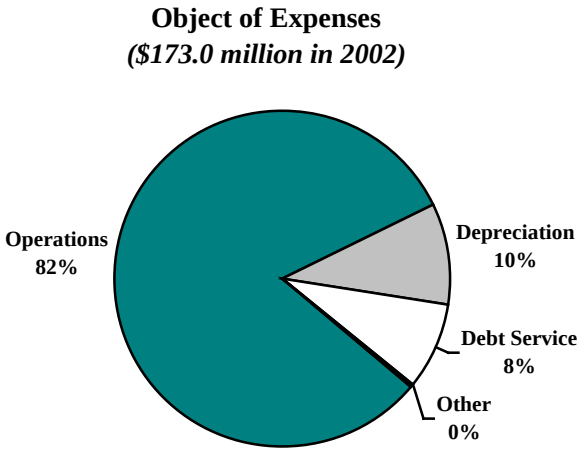
Service fees accounted for nearly two-thirds of CRRA's $157.5 million in operating revenues in FY 02.



Source of Data: CRRA Annual Financial Report

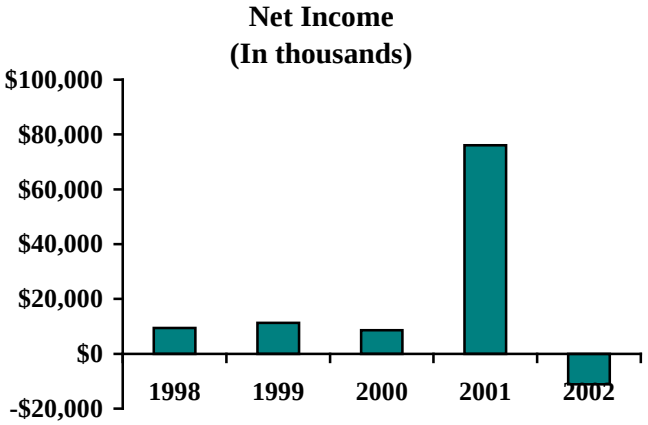
[1] The Governor with the advice and consent of the General Assembly shall upon request of a municipality served by a project appoint an ad hoc member (up to two per project) who shall vote only on matters concerning such project.

Operations consumed 82 percent of CRRA's $173 million expenditures in FY 02. Debt service payments accounted for 8 percent.



Source of Data: CRRA Annual Financial Report

In terms of total revenues (revenue from operations, investment income, settlement income, and other) and expenses (operating expenses, debt service, and other) data for FY 02 show a change in CRRA's financial health. It represents the only deficit the authority experienced over the last five years.

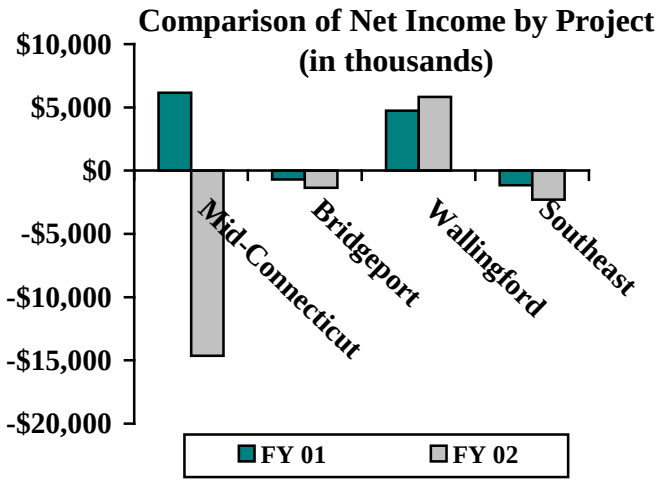


Source of Data: CRRA Annual Financial Report

In the figure above, the large increase in net income shown for FY 01 is primarily attributable to $60 million in settlement money CRRA received from the Connecticut Light and Power Company (CL&P) in connection with the restructuring of the state's electric industry. The FY 02 deficit is

due to a failed deal involving the Mid-Connecticut project and the Enron Corporation.

At the project level, the data show between FY 01 and FY 02, Mid-Connecticut went from an income surplus of $6.2 million to a $14.6 million deficit. Bridgeport's $705,000 deficit increased to $1.4 million. Wallingford's net income surplus increased from $4.7 million to $5.8 million. The Southeast project's deficit increased from $1.2 million to $2.3 million. Deficits are covered by reserves set aside for each project.



Source of Data: CRRA Annual Financial Reports

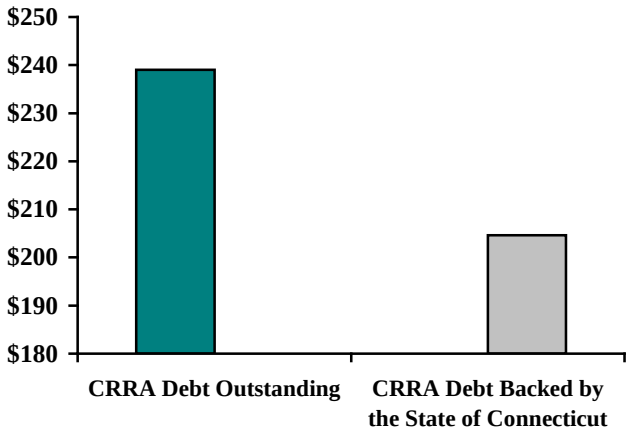
Bonding

CRRA is empowered to issue bonds to finance the design, development, and construction of resources recovery facilities and landfills.

The bonds issued by the authority are special obligation revenue bonds paid for by the money generated by the projects they support and other authority income.

Some of the bonds issued by the authority are backed by the state through what is known as the Special Capital Reserve Fund (SCRF). The amount of principal on the bonds outstanding as of June 30, 2002, was $239.0 million of which $204.6 million is covered by the SCRF.

Comparison of Total CRRA Debt Outstanding and the Portion Backed by the State (in $ millions)



Source of Data: CRRA Annual Financial Report

Table II-2 shows the bond principal outstanding at the project level as of June 30, 2002. The Mid-Connecticut project accounts for 87 percent of the debt, compared to less than 4 percent attributable to the Wallingford project.

Table II-2. Outstanding Principal by Project as of June 30, 2002 (in thousands)

Mid-CT	*Bridgeport*	*Wallingford*	*Southeast*	*Total*
$208,279	$12,245	$8,404	$10,051	$238.979

Source of Data: CRRA Annual Financial Report

CRRA's principal and interest payments will be roughly $40 million annually over the next 10 years.

Chapter Three

CRRA Problems

Enron

Background

In 1985, the Connecticut Light and Power Company and CRRA negotiated an energy purchase agreement, whereby CL&P would buy steam produced by the Mid-Connecticut project. The agreement set the price at the equivalent of $.085 per kilowatt hour. This was based on the rate CL&P charged municipal customers and was considerably above the market price. The contract ran through 2012, and provided CRRA with an annual revenue stream of nearly $40 million.

The electric restructuring act of 1998 encouraged CL&P to buy down its above-market power purchasing contracts. The act allowed the company to issue rate reduction bonds to raise the money it would need to accomplish this objective.

In 2001, in a complex arrangement involving CRRA, Enron Corporation, and CL&P, the latter bought its way out of the contract to purchase power from CRRA at an above-market rate. A summary of the key aspects of this wide-ranging three-party deal follows.

- CL&P financed the deal using $280 million from the sale of rate reduction bonds.
- CL&P made a lump sum payment of $220 million to Enron, which assumed CL&P's contract with CRRA to purchase steam produced by the Mid-Connecticut project.
- The 1985 CL&P-CRRA contract taken over by Enron was amended. The amended contract required CRRA to provide Enron an amount of steam sufficient to produce 250 million kilowatt hours of electricity per year. It called for Enron to pay CRRA a "capacity charge" equal to $2.2 million per month. The amended contract also required Enron to pay CRRA an additional $175,000 per month for the authority's unrestricted use.
- In a separate contract with CRRA, Enron agreed to pay CRRA to convert the steam into electricity at an initial rate of 3.1 cents per kilowatt hour (rising to 3.3 cents per kilowatt hour in 2004).
- Under another contract, Enron agreed to sell to CL&P 250 million kilowatt hours of electricity at the same price Enron paid CRRA for it.

- In a new contract with CRRA, CL&P agreed to buy any of the power produced by the Mid-Connecticut project above the 250 million kilowatt hours CL&P was already buying through Enron. Under the terms of this contract, CL&P would pay CRRA the same rate for the power as Enron was paying CRRA.
- In a related deal, CL&P paid CRRA $60 million, $10 million of which was immediately returned to pay for the purchase of CL&P's facilities and land located adjacent to the Mid-Connecticut site. Another $26 million went to purchase insurance for the environmental remediation of the site. The remaining money was put into a "Non-Project Ventures Fund" created by CRRA.

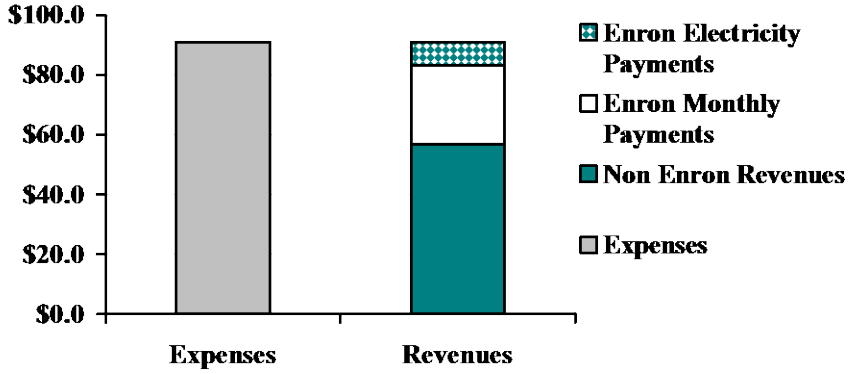
Essentially, Enron received money that CL&P owed CRRA under terms of the 1985 energy purchase agreement. Stripped of its complexity, the intent of the overall deal was to provide CRRA with enough money to offset the difference between what it would have received from CL&P under the original energy purchase agreement and what the authority would be paid under the reduced rate called for in the new agreement.

Consequences

In December 2001, Enron declared bankruptcy and stopped making all payments to CRRA.

The loss of Enron's $2.2 million monthly payments -- designed to make up the difference between the old above-market rate CRRA received for steam (the equivalent of $.085 per kilowatt hour) and the new rate for electricity ($.031 per kilowatt hour) -- reduces anticipated annual revenues for the Mid-Connecticut project by approximately $26 million.

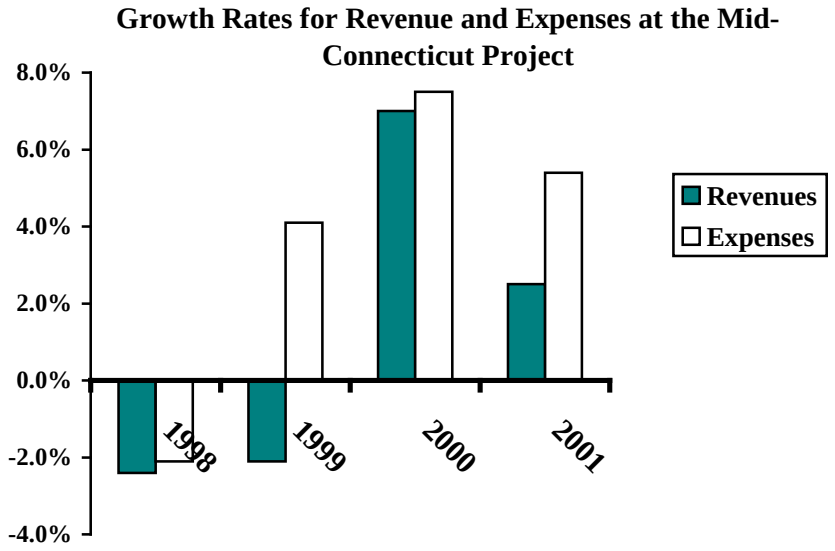
FY 02 Mid-Connecticut Project Estimated Expenses and Revenues including Enron's Share (in $millions)



Source of data: CRRA Annual Financial Report

The attorney general is preparing multiple lawsuits to recover the $220 million CL&P sent to Enron. However, even if the lawsuits are successful, it will be a long time before CRRA receives any money.

The Mid-Connecticut project's budget troubles are exacerbated by the fact that in the years preceding the Enron problem operating expenses had been growing at a faster rate than operating revenues.



Source of Data: CRRA Annual Financial Reports

Other Issues

Reporting

C.G.S. Sec. 1-122. Compliance audit. CRRA is required to have an outside auditor determine if the authority has conformed to state statutes and its own procedures.

- *CRRA was unable to provide compliance reports to the program review committee for fiscal years 1999 through 2001 meeting this requirement. A compliance statement was produced for 2002, but it was deficient in terms of the details required by the statute.*

C.G.S. Sec. 1-123. Annual Report. CRRA is required to prepare and distribute a report that includes: a list of new bond issues; net proceeds; firms involved and how the bonds were placed; a list of individuals and firms receiving in excess of $5,000 from the authority; a financial balance sheet; the cumulative value of all bonds issued, outstanding, and the state's contingent liability; the authority's affirmative action policy, description of the workforce, and the authority's affirmative action efforts; and the authority's planned activities for the current fiscal year.

- *The CRRA annual reports provided to the program review committee for fiscal years 1999 through 2001 addressed only some of the requirements. Missing from the reports were a list of outsiders paid more than $5,000, a discussion of the authority's affirmative action efforts, and a description of planned activities. These deficiencies were corrected in the 2002 report provided to the committee.*

C.G.S. Sec. 22a-263. Reports to governor and legislature. CRRA must report quarterly to the governor and annually to the General Assembly: the number and type of contracts entered into during the quarter; a listing of outstanding notes and bonds and the payment status; and the distribution of any surplus revenues.

- *CRRA provided no documents indicating quarterly reports meeting the requirements of C.G.S. Sec. 22a-263 were provided to the governor for fiscal years 2000 and 2001.*
- *The data CRRA provided or referenced indicated reports for the first three-quarters of fiscal year 1999 were filed, but they did not meet all of the statutory requirements, specifically data on the number and types of contracts were missing.*
- *There was no evidence indicating annual reports meeting the requirements of C.G.S. Sec. 22a-263 were filed with the General Assembly for fiscal years 1999 through 2002.*
- *A supplement to CRRA's 2002 annual report could be used to meet this requirement.*

Plan of Operations

C.G.S. Sec. 22a-264. Activities and operations. The authority must prepare an annual plan of operations, which shall be reviewed by the DEP commissioner for consistency with the state's solid waste management plan and approved by two-thirds of the authority's board.

- *During fiscal years 1999 through 2002 the authority did not produce a report meeting this requirement.*

Budget Preparation

CRRA is responsible for preparing and adopting separate budgets for each project. The authority's central office costs are allocated to the projects based the amount of time devoted to each project.

- *CRRA's Operations Division rather than the Finance Division prepared each project's budget for fiscal years 2002 and 2003. This approach removes a level of expertise and a significant independent check from the budget preparation process.*
- *CRRA's administrative budget is not prepared until after all project budgets are approved, forcing the use of estimates in allocating central office costs to projects.*

Procedures and Practices

C.G.S. Sec. 22a-264. Written procedures. The board of directors must adopt written procedures governing the authority's operations.

- *Despite changes in some of CRRA's operating procedures, since 1990 only the personnel (2002) and procurement policies (1994) were formally updated.*[2]

C.G.S. Sec. 22a-268a(3) CRRA's board is required to approve all non-budgeted expenditures in excess of $5,000.

- *CRRA's procedure calling for board approval of non-budgeted expenses in excess of $50,000 did not conform to the statutory provision*[3].

Personal Use of CRRA Resources

CRRA provided cell phones to 14 employees and vehicles and associated credit cards to at least 11 senior level staff.

- *In response to an independent audit CRRA adopted new procedures on the personal use of the authority's resources in October 2001. However, the new policy did not discourage the personal use of these items nor did it specify the time period within which an employee must reimburse the authority.*
- *There were no formal controls or oversight mechanisms in place to enforce compliance with the filing deadline or reimbursement of the authority.*

[2] In November 2002 the CRRA's new board of directors adopted a complete set of new policies and procedures.
[3] Revised procurement policies and procedures adopted November 21, 2002 conform to the statutory requirement.

Problems Identified in State Auditor Report

In October 2001, the state auditors released a report on CRRA. The audit covered the fiscal years ending June 30, 1998, 1999, and 2000.

The audit identified nine problems, six of which involved administrative controls. The problems along with the perceived cause are summarized in the table below.

Problem	***Contributing Cause***
CRRA failed to produce an annual plan of operation	Unable to determine
No assurance all fines levied by enforcement staff are collected	Lack of administrative controls and oversight
Absence of proper notification for changes in written procedures	Lack of administrative controls and oversight
Board chair's assumption of role not in conformity with the law	Authority and governor's office unaware or misinterpreted law
Absence of minutes of board subcommittee meetings	Lack of administrative oversight
Required set-aside goals and reports not submitted to proper agencies or were late	Lack of administrative oversight
Absence of a procedure to monitor compliance with requirement to reduce spending on outside consultants if CRRA staff exceeds 45	Authority regarded requirement as outdated
No board approval of employee severance agreements	Authority regarded board approval as unnecessary since funds came from budgeted salaries
Absence of reporting to assure provisions of contracts are upheld	Lack of administrative controls and oversight

Source: Auditors of Public Accounts, October 2, 2001 Report on CRRA

Problems Identified in the Media

During the time period when CRRA's troubles with the Enron deal were being reported a number of other issues surfaced in the media. Three of these revelations are recounted below.

- CRRA hired outside lobbyists including one who billed the authority for out-of-state trips to political functions and meals for the governor's staff.

- CRRA spent more than a million dollars to renovate and move into a new headquarters in downtown Hartford.

- CRRA diverted $60 million in settlement money from the Mid-Connecticut project to a newly created Non Projects Venture Fund, which was to hold the assets purchased with the funds and develop new businesses.

Conclusions

Based on the problems detailed above the program review committee concluded:

- *CRRA lacked the administrative controls and oversight mechanisms necessary to assure compliance with the authority's own policies and procedures; and*

- *CRRA operated under a management culture that ignored legislative policies and mandates and pursued its own interests in a somewhat ad hoc manner.*

Chapter Four

CRRA's Response to Problems

New Legislation

In response to issues surrounding the CRRA-Enron-CL&P deal and the other revelations surfacing at about the same time, legislation was passed making a number of statutory changes in the structure and responsibilities of CRRA.

Public Act 02-46 replaced CRRA's old board with a new 13-member board effective June 1, 2002. The key changes included increasing from two to five the number of municipal representatives, adding the state treasurer, and specifying criteria for non-government appointees.

A steering committee was created consisting of three to five board members jointly appointed by the governor, the president pro tempore of the Senate, and the speaker of the House. Among other responsibilities the committee was charged with:

- reviewing all aspects of CRRA's finances and administration;
- determining the financial condition of the authority and providing for mitigation of the impact on municipalities of the CRRA-Enron-CL&P deal;
- establishing a financial restructuring plan for the authority, subject to the approval of the board of directors; and
- submitting a report to the board and the General Assembly on the steering committee's findings and recommendations not later than December 31, 2002.

Under the act the attorney general was given the authority to supervise all legal matters and claims related to the CRRA-Enron-CL&P transaction.

The act made several changes in what CRRA can and cannot do. CRRA is:

- prohibited -- under C.G.S. Section 1-124 -- from issuing any debt backed by the state without the state treasurer's approval;
- allowed to borrow up to $115 million from the state;

- allowed to become an electric supplier, if approved by the Department of Public Utility Control;
- allowed to offer performance incentive plans, if they are based on both the performance of the authority and the person, applicable to all employees, and approved by the board; and
- prohibited -- along with all other quasi-public agencies -- from retaining lobbyists.

Actions taken by the new CRRA board

The new CRRA board held its first meeting on June 13, 2002. It immediately undertook several actions designed to deal with problems at CRRA.

- A mission statement was adopted that focuses the authority on its statutory responsibilities and emphasizes the importance of municipalities. As adopted, the authority's mission is:

  to work for - and in - the best interests of the municipalities of the state of Connecticut in developing and implementing environmentally sound solutions and best practices for solid waste disposal and recycling management on behalf of municipalities.

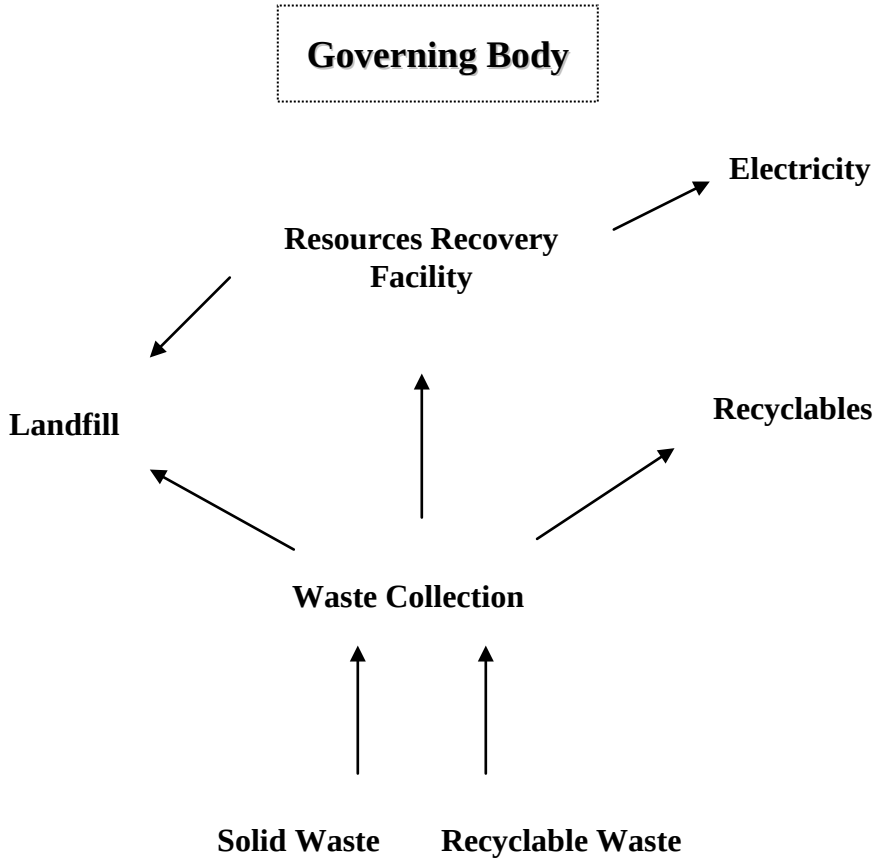
- Policies and procedures were reviewed and rewritten by subcommittees of the board and adopted by the full board in November 2002. Among the changes are:
  - *assignment of vehicles to individual employees was ended and the use of vehicles was restricted to business matters as was the use of cell phones;*
  - *assignment of credit cards was changed from individuals to vehicles and personal use of the cards was prohibited; and*
  - *procurement practices were changed in a manner that puts greater emphasis on board oversight.*
- The board hired a new president and chief financial officer.
- The board has cooperated with the attorney general to aggressively seek recovery of the money lost in the Enron deal.

- The board has engaged a consultant to explore the feasibility of consolidating its headquarters on one floor and subleasing the other floor.
- The legal firm that represented CRRA throughout its existence has been replaced.
- Contracts for professional services such as an insurance brokerage firm, financial auditor, and bond counsel have been put out to bid.
- Money in the Non-Project Ventures fund was designated for return to the Mid-Connecticut project.

Chapter Five

Solid Waste Management Models

Components of a Basic System



Governing Body -- Entity with the responsibility and authority to set policy and manage the solid waste disposal system. This can be an agency of state or local government, a quasi-public agency set up by a state or local government, or a private company.

Waste collection -- Generally, municipalities make arrangements to have waste including recyclables picked up. In some cases they may use their own department of public works, in others they may contract with private haulers or approve private haulers with whom the public may contract for waste removal.

Resource Recovery Facility -- Place where burnable waste is deposited and incinerated to heat water and change it into steam, which in turn powers turbines that generate electricity.

Landfill -- Place where waste that cannot be burned and ash residue resulting from the combustion cycles in waste-to-energy plants are deposited.

Recycling Center(s) -- Place where materials such as glass, newspaper, and various metals that can be reprocessed into useful articles are deposited and depending on the market either sold or given away.

Models

Government Agency

Under the government agency model a unit of municipal, county, or state government has responsibility for the disposal of solid waste. The entity could be a separate agency or division of a larger agency. It operates in the same manner as other public agencies and is subject to such controls as the governmental budget process, personnel system, and procurement procedures. Two examples of this model were found in Florida -- City of Tampa and Pinellas County.

Components	***Tampa***	***Pinellas***
Governing Body	City Government	Board of County Commissioners
Governing Body Staff	City employees including haulers	County employees
Owner of Waste to Energy Facility	City	County
Operator of Waste to Energy Facility	Private Company (Wheelabrator)	Private Company (Wheelabrator)
Financing	Government Bonds	Government Bonds
Operating Budget	$45 million	$31 million
Tipping Fees	Set by city budget on a fee for service basis, not tonnage	Set by Board of Commissioners $37.50 (ton)
Annual Capacity (tons)	320,000	970,000

Quasi-Public Agency

Under the QPA model an agency is created as a political subdivision by one or more municipalities, a county, or state for the specific purpose of managing a district's solid waste disposal system. The agency functions as a private entity free of most controls imposed on government agencies, although the agency is subject all to the regulations that apply to a private company engaged in the same activities. The entity's powers are spelled out in its enabling statute. Responsibility for exercising those powers resides with a board of directors whose members are appointed by elected officials.

The quasi-public agency model is the most prevalent arrangement for managing solid waste disposal systems found in the nation. CRRA and the waste to energy system centered in Bristol are prime examples of state and municipal QPAs. These two approaches are compared in the table below.

Components	***CRRA***	***Bristol***
Governing Body	Board appointed by state officials	Board appointed by officials of the 14 towns served
Governing Body Staff	55 (estimate)	5
Owner of Waste to Energy Facility	CRRA	Private Company
Operator of Waste to Energy Facility	Private Companies	Private Company
Financing	Government Bonds	Government Bonds
Operating Budget	$180 million	$21 million
Tipping Fees	$55 - $69 per ton includes recycling	$61 per ton solid waste plus $33 per ton recycling
Annual Capacity (tons)	153,000 - 880,000	180,000

Private Sector

Under the private sector approach a private company designs, constructs, owns, and operates the resources recovery facility. The burden is on the company to find and sign contracts with municipalities and other customers to provide waste. The tipping fees are set by the contracts, most of which are long term or the spot market. The fees generally vary based on market conditions at the time the contract is signed. Beyond environmental regulation there is little governmental involvement in the operation of the system. It is up to the private company to keep the facility operating. Municipalities under this model typically handle recycling separately.

Examples of privately operated systems were found in Massachusetts. All of the instances involved a single company, Waste Management.

Components	***Massachusetts (Composite)***
Governing Body	Private Company
Governing Body Staff	Unknown
Owner of Waste to Energy Facility	Private Company
Operator of Waste to Energy Facility	Private Company
Financing	Private (Possible to use government bonds if tied to a public purpose economic development project.)
Operating Budget	Unknown
Tipping Fees	$50 - $67 per ton
Annual Capacity (tons)	74,000 - 835,000

Chapter Six

Comparison of Models

Creation of CRRA

Public Hearings

At the time of CRRA's creation in 1973, it was viewed as an experimental approach to dealing with the state's solid waste crisis. However, the proposal did not come without reservations. These can be summarized as:

- lack of citizen input;
- insufficient municipal representation on the authority's board of directors;
- lack of legislative control over the authority particularly in the use of bonds that would be backed by the state;
- potential for misuse of eminent domain powers by the authority;
- possibility of no-bid contracts;
- possibility for profits made by the authority not being returned to the state or taxpayers; and
- possibility of municipalities being forced into joining the authority.

Legislative Debate

In the House, debate centered on using state controls to tie the solid waste management authority closer to state government. Similar concerns were debated in the Senate, which considered but rejected an amendment requiring employees of the new authority to have the same rights and responsibilities as state employees.

While there seemed to be many arguments for creating a stronger tether between the authority and the state, there was never an overwhelming argument for using the private industry approach to deal with Connecticut's solid waste management crisis.

Alternative Models

Alternative models for operating waste management systems can be placed on a continuum based on the amount of control exerted by elected officials.

While in theory a number of models can exist on this continuum, only the three alternatives listed below are reviewed in this report.

1. State agency managed and privately operated solid waste disposal system.
2. Quasi-public agency managed and privately operated solid waste disposal system.
3. Privately managed and operated solid waste disposal system.

Criteria for Comparing Models

The five categories described below can be used to facilitate a comparison of the three models. The comparisons shown in the tables that follow represent a homogenization of the literature and the opinion of the program review committee and its staff.

- Accountability -- holding entities responsible for their performance;
- Management flexibility -- nature of constraints on personnel and financial matters;
- Access to capital -- degree of difficulty in raising the money in the financial markets;
- Price setting -- process for setting tipping fees; and
- Innovation -- nature of the incentives to seek and adopt new technologies and processes.

Accountability

State Agency	Quasi-Public Agency	Private Company
Responsibility for actions of the agency rests with its head, who is accountable to the governor. A citizen's recourse is to vote for or against the appointing authority.	Responsibility for actions of the agency rests with its head, who is accountable to a board of directors, which is appointed by and accountable to multiple elected officials. A citizen's recourse is to vote for or against appointing authorities.	Responsibility for actions of the company rests with its head, who is ultimately accountable to the owners of the company. A citizen's recourse is to take his or her business elsewhere.

Management Flexibility

State Agency	Quasi-Public Agency	Private Company
Personnel and procurement decisions are rule based and constrained by external authorities.	Personnel and procurement decisions are based on the tasks needing to be performed.	Personnel and procurement decisions are based on satisfying customers in the marketplace.
Financial management is focused on the budget process, which is controlled by external authorities.	Financial management is focused on balancing costs and revenues.	Financial management is focused on cutting costs and increasing revenues.

Access to Capital

State Agency	Quasi-Public Agency	Private Company
Funds come from state appropriations and the sale of bonds. The agency must compete with other state priorities for the funds.	Funds come from revenues generated by the agency and selling bonds. In the case of the bonds, the agency may face limits if the state runs up against caps on tax-exempt borrowing.	Funds come from project revenues, sale of stock, issuing of bonds, or borrowing against future earnings.

Price setting

State Agency	Quasi-Public Agency	Private Company
Tipping fees are determined through a political process. The fees may include subsidies or overcharges.	Project costs determine the tipping fees. The fees are set to bridge the gap between revenues from other sources and agency expenditures. However, market forces can exert downward pressure on rates.	The market determines the tipping fees. If it is a highly competitive market, fees will be pushed as low as needed to attract customers. If the market is monopolistic, fees will be set to maximize the company's profits.

Innovation

State Agency	Quasi-Public Agency	Private Company
Procurement rules, the budget process, and the political system's risk averse nature often combine to stifle technology development and innovation.	Free of many state government constraints, quasi-public agencies are inclined to take risks associated with innovation.	The rewards derived from improved efficiency give private companies an incentive to innovate. They often allocate money for research and development. Private companies also tend to have a culture that rewards risk taking.

Advantages and Disadvantages

The data provided in the above categorical comparisons can be used to identify the advantages and disadvantages of each model. The major benefits and drawbacks of each are summarized below.

State Agency Model

Advantages

- All assets are under public control.
- Control over what is essentially a citizen service including planning, operating, setting prices, and regulating is centralized in state government.
- Focus on fairness and equity in matters relating to personnel and procurement is maximized.
- Accountability for performance is centralized in the political system.

Disadvantages

- Demands on state resources are maximized.
- State liabilities are maximized.
- Ability to respond quickly to changing market conditions is constrained by the state bureaucracy and risk averse approach.
- Incentive to innovate is minimal.

Quasi-Public Agency Model

Advantages

- Most governmental rules impacting the agency's operation are eliminated allowing it to be run like a business.
- Demand on state resources reduced.
- Innovation and risk taking is possible.
- Accountability remains loosely under political control through the agency's statutory charter and the system for appointing members of the board of directors.

Disadvantages

- State maintains a high level of responsibility without corresponding level of authority.
- Incentives to hold costs in check are weak since tipping fees -- within in reasonable limits -- can be set to cover any gap between costs and revenues.
- Although reduced, state liabilities remain significant.

Private Company Model

Advantages

- State liabilities are minimized.
- Responsiveness to changes in market conditions are maximized, assuming a competitive market exists.
- Incentives to innovate and take risks to reduce costs are maximized.
- Taxes are paid on property, income, and sales.

Disadvantages

- State regulatory responsibilities are increased.
- State maintains limited expertise.
- Loss of control by political system over what has traditionally been a government responsibility.

Issues related to changing models

The advantages and disadvantages listed above are useful within the context of implementing a management model where none exists. When the question is whether to change from the current quasi-public agency model to either of the other models a major problem arises.

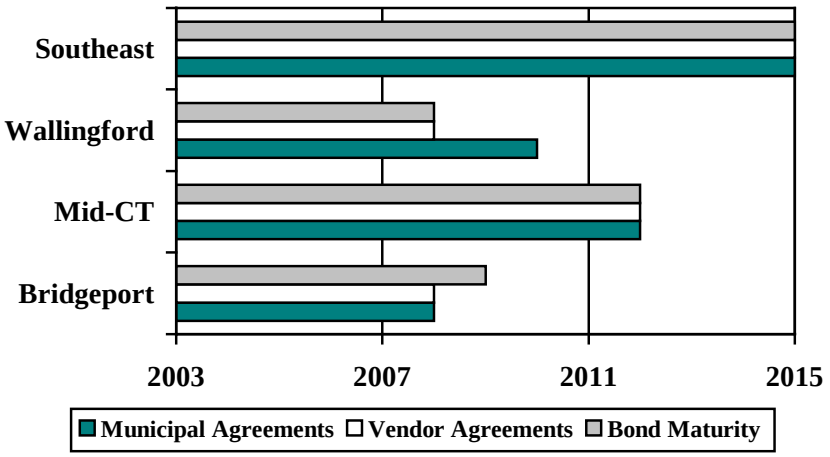
The problem is related to CRRA's organizational structure, which involves four separate projects each with a unique legal, financial, and operational structure. The issue is rooted in the fact controlling the operation of each project are agreements between the authority and the participating municipalities, vendors, and bondholders.

As shown in the figure below the termination dates for these agreements vary among the projects from 2008 to 2015. As a result of these factors the committee finds:

- *changing the state's management model for solid waste disposal from a quasi-public agency to either a state agency or private sector model would have to be done on a project-by-project basis; and*

- *changing the state's management model for solid waste disposal from a quasi-public agency to either a state agency or private sector model prior to 2015 would require renegotiating existing agreements with municipalities, vendors, and bondholders.*

Year of Termination for Major Agreements by Project



Effect of project agreements

The program review committee concludes changing CRRA from a quasi-public to a state agency prior to the scheduled termination of the type of agreements identified above would, at the very least, require the consent of the parties to the agreements or their representatives. Specifically, the committee finds:

- *in the case of a conversion to a state agency, each project's municipal service agreements, although allowing for a change in the authority's structure, would require the consent of the project's municipalities;*
- *vendor contracts scheduled to be in effect beyond the date of a change to a state agency would have to be renegotiated; and*
- *trustees for the various outstanding bond obligations would need to be assured the change to state agency status would not jeopardize the rights of bondholders.*

Similarly, the committee concludes if CRRA was eliminated and its function taken over by the private sector prior to the scheduled termination of the agreements, approval of the parties to key project agreements would be needed. Specifically, the committee finds:

- *turning CRRA's function over to the private sector prior to the scheduled termination of existing municipal service agreements would require negotiations with the municipalities to end such agreements;*
- *turning CRRA's function over to the private sector prior to the scheduled termination of existing vendor agreements would require negotiations with vendors to end such agreements; and*
- *turning CRRA's function over to the private sector would require all outstanding bond issues to be defeased.*

Recommendations pertaining directly to CRRA

Based on the analysis and findings cited above the program review committee makes the following recommendations.

CRRA should be continued as a quasi-public agency through at least 2008.

At least three full years prior to the scheduled termination of the municipal service agreements governing a project, the CRRA board should form a special committee consisting of representatives of the authority and all municipalities involved in the project to develop options for disposing of solid waste at the conclusion of the existing agreement.

The options analyzed by each special committee should include turning the function over to the private sector.

Discussion

In the view of the program review committee, renegotiating existing agreements would be a difficult task to accomplish in the near-term. Time would be needed to assure all parties involved they would, at the very least, not be any worse off after a change.

While a state takeover would provide stability, it raises concern about how responsive a bureaucracy, with its own set of objectives and accountable to the state, would be to the needs of municipalities.

Turning over the operation to the private sector could be even more unsettling to municipalities and require considerable time and effort to assure their interests would not be harmed. The key would be the amount of money received from the sale of CRRA's assets and how the cash was distributed. Though time consuming, negotiations probably would succeed if the money raised by the asset sale was sufficient to defease the bonds and provide funds for municipalities to ease the transition to a competitive private sector market.

Studying options prior to the termination of the agreements surrounding projects is not a new idea. CRRA has already contracted for such studies of the Bridgeport and Wallingford projects, which are scheduled to end in 2008. In addition, CRRA has agreed to support an independent study of the Bridgeport project that will take place under the direction of the project's participating municipalities.

Chapter Seven

Quasi-Public Agencies other than CRRA

Agencies designated as quasi-public by the state are identified in C.G.S. Section 1-120. They include the Connecticut Development Authority (CDA), Connecticut Innovations Incorporated (CII), Connecticut Health and Educational Facilities Authority (CHEFA), Connecticut Higher Education Supplemental Loan Authority (CHESLA), Connecticut Housing Finance Authority (CHFA), State Housing Authority (SHA), Connecticut Resources Recovery Authority, Connecticut Hazardous Waste Management Service (CHWMS), Connecticut Port Authority (CPA), Capital City Economic Development Authority (CCEDA), and Connecticut Lottery Corporation (CLC).

The Connecticut Port Authority and State Housing Authority -- formerly the Connecticut Housing Authority and now a subsidiary of CHFA -- have been excluded from this stage of the review because they do not function as traditional quasi-public agencies. Their staff needs are met by other agencies and neither authority currently issues bonds.

Other Quasi-public agencies compared to CRRA

Media stories surrounding CRRA concerning employee bonuses, severance agreements, and personal use of the authority's resources raised questions about the state's other quasi-public agencies. As a result, an analysis of selected practices of their operations was included in the committee's scope of study.

A survey of QPAs by the Office of Legislative Research (OLR) conducted in the spring of 2002, provided information on executive pay, personal use of vehicles, bonuses, and employee severance agreements. The results were contained in a report issued June 10, 2002 (2002-R-0518).

An analysis by the program review committee of the data made available by OLR found the following.

- *CRRA topped the list for compensation (salary and bonuses) for authority heads, paying its chief executive $193,000 in FY 01. This was $33,000 more than the next highest paid chief executive and $65,500 above the average for chief executives of the other QPAs.*

- *Seven of the nine QPAs paid employee bonuses in FY 01. As a percentage of operating expenses the bonuses ranged from one-tenth of 1 percent to 1.8 percent. Five of the agencies, including CRRA, were clustered around one-tenth of 1 percent.*
- *Two of the four former QPA employees reported to have received additional benefits in their severance agreements were from CRRA.*
- *One of the two non-disparagement agreements in effect involved a former CRRA employee.*

Based on these results, the committee finds:

- *CRRA operated at the edge of the curve for the other quasi-public agencies in awarding executive compensation and negotiating severance agreements.*

The program review committee conducted its own survey in the fall of 2002 on the practices of QPAs regarding personal use of vehicles, cell phones, and credit cards. The results are summarized in the table below.

	Are the following items provided to employees for round-the-clock use?			***Are there written policies addressing reimbursement for personal use?***		
Quasi-Public Agency	***Vehicles***	***Cell phones***	***Credit Cards***	***Vehicles***	***Cell Phones***	***Credit Cards***
CRRA *(a)*	Yes - 11	Yes - 14	Yes -11	No (b)	No (b)	No (b)
CDA	Yes - 2	Yes - 4	Yes - 3	Yes	Yes	Yes
CII	No	Yes - 17	Yes - 8	N/A	Yes	No (c)
CHEFA	No	Yes - 1	Yes - 9	N/A	No	Yes
CHESLA	No	No	Yes - 2	N/A	N/A	No (c)
CHFA	Yes - 1	Yes - 6	Yes - 2	Yes (d)	Yes	Yes
CHWMS (e)	No	No	No	N/A	N/A	N/A
CCEDA	No	Yes - 5	No	N/A	Yes	N/A
CLC	Yes - 41	Yes - 53	Yes - 8	No (c)	No (c)	No (c)

a) Data reflect conditions prior to policy changes instituted in the fall of 2002. Written policies are now in place for use of cell phones, credit cards, and vehicles, with the latter two no longer assigned to individual employees.
b) Policy did not specify time period for reimbursement
c) Policy prohibits personal use.
d) Personal use reported as income at a rate of 34.5 cents per mile.
e) Functioning in a limited capacity.

The data in the above table show, with the exception of CLC and CII -- which have large field operations -- the use of vehicles, cell phones, and credit cards is not as extensive as it was at CRRA prior to recent changes there. In addition, policies covering reimbursement for the personal use of such items appear to be in place in nearly all instances. Based on this analysis the program review committee finds:

- *the reimbursement policies now in effect at quasi-public agencies governing the personal use of vehicles, cell phones, and credit cards preclude the need for legislature action.*

The reimbursement policies noted in the table above were set by an authority's board in some instances and by its executive staff in others. While this does not constitute a major problem, the committee believes it would be prudent for the board of directors of each QPA to adopt written policies governing the use of these items. Therefore, the committee recommends:

the board of directors of each quasi-public agency identified in C.G.S. Section 1-120, if it has not already done so, should adopt written policies governing the use of vehicles, cell phones, credit cards, and such other items as the board deems necessary.

Quasi-public agency reporting requirements

C.G.S. Section 1-122 (Annual Compliance Audit) and Section 1-123 (Annual Report) detail public reporting requirements for quasi-public agencies. The reports are intended to provide government officials and the public important information on the activities and practices of quasi-public agencies.

The committee reviewed the most recent annual and compliance reports of each QPA. It found the annual reports and supplemental information provided by QPAs to designated recipients generally meet the requirements of C.G.S. Section 1-123.

However, the same cannot be stated about the compliance reports. Intended to be an independent review of whether a QPA complied with its own procedures and state laws, the reports, in the opinion of the committee, were completely inadequate to meet this purpose.

In all instances, the agency's financial auditor issued a letter containing a paragraph similar to the example below taken from CRRA's report.

> "As part of providing reasonable assurance about whether [CRRA's] financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, grants, and [C.G.S.] Section 1-122, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of the audit, and accordingly, we do not express such an opinion. However, our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards."

The General Assembly does not have a formal procedure in place for tracking and assessing reports required of quasi-public agencies. On an informal basis, the legislative library staff logs in the reports and follows up on those not submitted. However, the library lacks the mandate and resources necessary to evaluate whether the reports meet all of the statutory requirements.

Based on its review of the reports and the mechanisms in place to assure they are submitted to the appropriate officials and meet requirements of the statutes, the committee finds:

- *the state's quasi-public agencies are not in compliance with the spirit of C.G.S Section 1-122, or in selected instances the requirements of C.G.S. Section 1-123, governing the reporting of information to the General Assembly and public; and*
- *noncompliance with reporting requirements by quasi-public agencies is made possible by the General Assembly's lack of a formal system to track and assess reports required of quasi-public agencies.*

To address these findings, the committee recommends the following:

> **The reports required by C.G.S. Section 1-122 and Section 1-123 should be submitted to the Legislative Program Review and Investigations Committee for an assessment as to whether the reports meet the statutory requirements. Within 30 days of receiving a report, the program review committee should notify those designated to receive the report of its availability and the committee's assessment of the report's compliance with legislative intent.**

A related issue is the independence of a quasi-public agency's compliance and financial auditors. In the view of the program review committee:

- *critical data on the financial activities and operational practices of quasi-public agencies is not developed by sources independent of the agencies.*

While the current arrangements are perfectly acceptable in the private sector, the agencies in question are quasi-public not quasi-private. As such, the public needs to have confidence the financial and operational practices of quasi-public agencies are being audited and reported precisely and unambiguously.

In the opinion of the committee, the best way to accomplish this is to ensure the independence of the auditors. Therefore, the program review committee recommends the following:

> **The State Auditors of Public Accounts shall be responsible for performing or contracting for the performance of all compliance and financial audits of the quasi-public agencies identified in C.G.S. Section 1-120. Each quasi-public agency shall annually pay the state auditors for the cost of the audits, whether performed by in-house audit staff or through a contract with an outside audit firm.**

The cost of the financial and compliance audits reported to the program review in the survey of QPAs ranged from $5,000 to $48,000 and totaled nearly $240,000. However, the audit costs would likely be higher in order to pay for the type of compliance report required by C.G.S. 1-122 and not now being produced.

APPENDICES

CHESLA

www.chesla.org

Connecticut Higher Education Supplemental Loan Authority
342 North Main Street, Suite 202, West Hartford, Connecticut 06117
(860) 236-1400 Outside CT • (800) 252-3357 In CT • FAX (860) 236-0910

January 14, 2003

Mr. George W. McKee
Chief Analyst
Legislative Program Review and
Investigations Committee
State Capitol
Room 506
Hartford, Connecticut 06106

Dear George,

I am sending this letter on behalf of the Connecticut Higher Education Supplemental Loan Authority (CHESLA) in response to the Legislative Program Review and Investigations Committee's final report on CRRA and other Quasi-Public Agencies.

After reviewing the January 2003 Final Report, the major impact to CHESLA will be to require an additional compliance audit under CGS 1-122, as the committee finds insufficient the current practice of relying on the review performed as part of the financial audit. Obviously, this would be an additional cost to the Authority. The recommendation also calls for the State Auditors of Public Accounts to perform or contract for the performance of all compliance and financial audits, with each quasi-public agency paying for its respective audits. One concern here is that CHESLA has just entered into a contract for its independent financial audit and for a program audit of its loan program servicer. The Authority should not be obligated to pay for two such audits.

Additionally, the report suggests that the reports prepared pursuant to CGS 1-122 and 1-123 be reviewed annually by the committee, with the committee to advise those designated to receive the report of its availability and compliance with legislative requirements. Our concern here is that any determination of non-compliance should not interfere with required NRMSIR filings, and that any such finding should not constitute a "material event" within the meaning of the Continuing Disclosure Agreements to which the Authority is a party.

The report gives the impression that the quasi-publics operate completely without any state oversight. (See Table I-1.) I would like to point out the additional CHESLA functions subject to external controls:

Bonding – requires approval by the State Bond Commission (through requirement of allocation of Private Activity Volume Cap) and requires approval of the State Treasurer (as part of use of SCRF, see CGS 1-124);

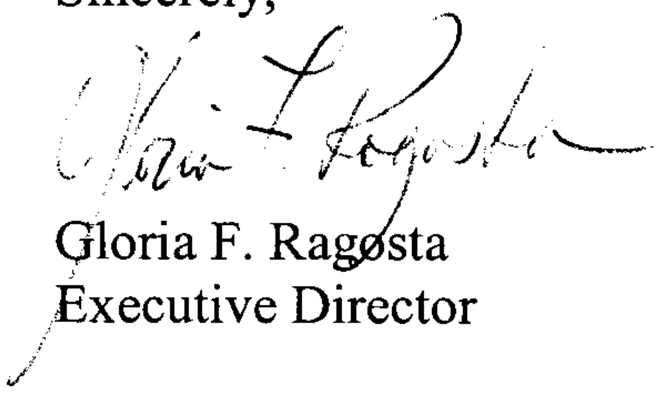
Contracting – requirement of going out for bids every three years, including additional limitations regarding finder's fees and third party payments;

Affirmative Action – adoption of regulations and procedures – although not subject to UAPA, we are subject to CGS 1-121 and 30 days' notice in the Connecticut Law Journal.

It should be made clear, that quasi-public agencies are not without any limitations or oversight on these points, as the table in the report would lead one to believe.

Thank you for the opportunity to submit an addendum to the Committee's Report.

Sincerely,



Gloria F. Ragosta
Executive Director

Cc: Senator Joseph Crisco, Co-Chair
Representative Julia Wasserman, Co-Chair
CHESLA Board
Judith Blank, Esquire, DB&H
Martin Budd, Esquire, DB&H

CHEFA
CONNECTICUT HEALTH AND EDUCATIONAL
FACILITIES AUTHORITY

January 21, 2003

Mr. George W. McKee
Chief Analyst
Legislative Program Review and Investigations Committee
State Capitol
Room 506
Hartford, Connecticut 06106

RE: Response to *CRRA and other Quasi Public Agencies Report* – January 2003

Dear Mr. McKee:

This letter is a response to the above-referenced report on behalf of the Connecticut Health and Educational Facilities Authority (CHEFA). I will confine my responses to the material contained on page ii in the Digest section and pages 37-39 in Chapter 7 of the report.

I must respectfully but strongly disagree with the report's conclusion that CHEFA is in non-compliance, spiritual or otherwise, with C.G.S. 1-122 and C.G.S. 1-123.

I am aware that no specific representation was made relative to CHEFA's non-compliance but it was included under a general statement of non-compliance by all quasi-public agencies, and therefore a reader of the report could reasonably conclude that CHEFA does not meet the requirements of the statutes. It is my opinion that such a broad based statement is a material weakness in the report and does a great disservice to CHEFA.

CHEFA, on an annual basis, prior to September 28 of each year, submits a report to the Governor of the State of Connecticut with copies sent to the Auditors of Public Accounts, the Co-Chairs of the Joint Committee on Finance Revenue and Bonding, the Connecticut State Library, and the Legislative Library. The most recent submission dated September 19, 2002 ran over 115 pages in length and described every aspect of CHEFA's operations for the previous fiscal year, and contained an extremely detailed budget approved by the CHEFA Board of Directors and its approved Strategic Business plan for the next several fiscal periods. Included in the Strategic Business Plan is a detailed analysis of CHEFA goals, objectives and strategies for the previous fiscal year and the extent of which the goals of CHEFA have or have not been met.

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The September 19, 2002, submission includes financial statements with unqualified opinions and management letter that states there were no material areas of non-compliance and no material financial weaknesses noted. The Auditors of Public Accounts review CHEFA operations on a two-year cycle. The last two reports spanning a period of the last four fiscal years contained no recommendations that were not implemented. When the Auditors of Public Accounts made a recommendation relative to increasing the reporting to the Legislature on state liability under the Special Capital Reserve Fund program three reports ago, it was immediately accepted and adopted as policy by CHEFA.

In addition to the reports required under the statute, CHEFA regularly prepares reports on all of its market sectors that are available and have been provided to the General Assembly and the public alike.

Prior to the issuance of any revenue bonds as required under federal law, CHEFA publishes in a variety of local newspapers a notice of each transaction which includes the name of the institution, the anticipated amount of the bond, and the projects for which the funds will be expended. This notice also informs the public that it may submit written testimony against or in support of the transaction and may provide oral testimony during a public hearing (TEFRA Notice). These notices are published in English and Spanish in order to allow for the broadest possible range of input from the public prior to presentation to the CHEFA Board, and if approved, to the Governor for final sign-off.

In addition, all activities of CHEFA can be accessed by the public on its website at www.chefa.com. Examples of information available at this site include financing forecasts, TEFRA notices, annual financial statements, and summaries of previous CHEFA bond financings and minutes of Board and Committee meetings.

In my opinion CHEFA complies with not only the letter of the statutes but goes far beyond what us required by statute in the disclosure of its operations and its policies both on the existing statutory schedule but also on an on-demand basis.

I wish to address the two recommendations contained in the report and explain that while in some cases they are not feasible and in some cases may cause a significant disruption of the normal bond issuance process at CHEFA.

Submission of the reports to the Legislative Program Review and Investigations Committee with a 30-day review period given the September 28 deadline is not feasible. The audited financial statements for the CHEFA year end of June 30 are not available and final until accepted by the Board of Directors at the regular Board meeting schedule for the second Tuesday in September. This leaves insufficient time for the review as recommended in the report and compliance with the September 28 statutory deadline for submission to the parties of interest.

In my conservative opinion on these matters, an assessment of compliance by the Legislative Program Review of Compliance creates, in the event of the determination of non-compliance, an event that must be disclosed during the sale of new bonds and to secondary market investors under SEC rules. Such a determination based upon opinion as

stated in this report would also be contradictory to the formal and authoritative unqualified opinion of the CHEFA outside auditors and Statement of No Recommendations by the Auditors of Public Accounts.

Relative to the second recommendation regarding compliance issues, it should be noted that the Auditors of Public Accounts, when conducting an audit at CHEFA, already test compliance with state requirements such as purchasing and hiring. As previously stated, the Auditors of Public Accounts and have as states previously for the past two years made no recommendations to CHEFA.

In my opinion there is an implication in this report that outside auditors would be involved in the development of financial and operational procedures. This obviously is totally outside the scope of an audit which tests procedures created by the governance and staff of a quasi-public authority and does not participate in their creation. If this matter were pursued, I as Chief Executive Officer might be required to make representations and warranties as part of the audit as to procedures to which I was opposed. The obvious conflict of interest would not allow me to make such representations and warranties.

If this recommendation were enacted into law I would recommend that CHEFA not terminate its contract with an outside firm and subsequently CHEFA would be required to expend two audit fees rather than one. The public finance market and CHEFA clients have come to expect an independent outside audit and termination of same could have a negative effect on the bond issuance process.

In closing, the tragic loss of taxpayer money by the Connecticut Resources Recovery Authority was a result of an environment which was, in my opinion, unique to that organization. I can categorically state that such a loss could not currently occur at CHEFA given the conservative policies and procedures in place at this Authority. A determination such as contained in the report that CHEFA is not in compliance with statutes is, in my opinion, erroneous. The limited freedom from government regulation granted to CHEFA is more than justified when compared with the advances in healthcare, education, and childcare that have been made as a result of CHEFA financing and grant programs. I look forward to the continuation of the debate on this matter.

Sincerely,

Richard D. Gray
Executive Director

cc: Senator Joseph Crisco, Co-Chair
Representative Julia Wasserman, Co-Chair

Connecticut Innovations

APPENDIX C

January 20, 2003

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Mr. George McKee, Chief Analyst
Program Review & Investigations Committee
Room 506
State Capitol
Hartford, CT 06106

Dear Mr. McKee:

I write this letter on behalf of Connecticut Innovations, Inc. and the Connecticut Development Authority. Please consider this letter our formal agency response to the Program Review and Investigations Committee's final report on CRRA and other Quasi-Public Agencies.

My comments relate to Chapter 7 only, as this is the chapter dealing with quasi-public agencies in general. In the broad view, I believe very little new information about the state's quasi-public authorities was revealed in this study. Much of the information was a summary of data provided by the quasi-public authorities to the legislature's Office of Legislative Research earlier in the year.

The committee recommendation that the board of directors of each quasi-public authority adopt written procedures governing the use of cell phones, credit cards and company vehicles does not impact either CI or the CDA as both authorities' boards have already adopted such procedures. There are other statements and recommendations made in the report, however, that we believe misrepresent the record of both CI and the CDA. As such, we wish to have our response to these statements become part of the final report.

Every year, both CI and the CDA contract with outside, independent auditors to conduct our statutory financial and compliance audits. As is required by statute, the results of these audits are shared with the Governor, the state Auditors of Public Accounts and the legislature's Commerce Committee. Both CI and the CDA have a favorable record for consistently filing these reports with the legislature and for doing so in a timely manner. In the biennial audit performed by the Auditors of Public Accounts neither authority has been cited for not filing these statutory reports or for filing reports that are inconsistent with the requirements of the statute.

Based on our record, therefore, we take exception to the characterization that we are not in compliance with the spirit or requirements of the law. While you did not name CI or the CDA specifically as those authorities not complying with the requirements of the law, your statement paints all quasi-publics with a broad brush and leads the reader of the final report to believe that CI and the CDA are noncompliant.

You continue by questioning the independence of the outside auditors used by the quasi-public authorities to conduct financial and compliance audits. It is the opinion of the committee that the outside auditors are not independent of the authorities and as such, the public does not have confidence in the financial and compliance audits being performed. Your solution to this is to make the Auditors of Public Accounts responsible for performing or contracting for the annual financial and compliance audits.

It should be noted that state statute requires CI and the CDA to solicit proposals for professional services (i.e. outside auditors) at least once every three years. Additionally, state statute requires that the board of directors of CI and the CDA adopt written procedures relating to contracting for professional services used

by the authority. These statutory requirements help ensure that the professional services we receive are necessary, reasonably priced and in the case of our outside auditors, independent of the organization.

I would point out that the state Auditors of Public Accounts already have statutory authority to audit, as frequently as deemed necessary, all of the books and accounts of the quasi-public authorities. This audit may include an examination of performance to determine each authority's effectiveness in achieving its legislative purpose. Being that the Auditors of Public Accounts already have this statutory authority it is unlikely that the committee's recommendation to make the Auditors of Public Accounts responsible for the financial and compliance audits as well will do anything to improve public confidence. In fact, it appears that, contrary to your goal, you are decreasing the independence of the audits by consolidating all responsibility in one place.

Both CI and the CDA have had over the years a good working relationship with the Auditors of Public Accounts. Our comments are in no way intended to minimize the important role they play in the auditing process or to be critical of the level of expertise they bring to the audit. However, passing legislation requiring the Auditors of Public Accounts to perform or contract for our audits will have unintended consequences. Because of the nature of our businesses, CI and the CDA would still have to hire outside independent auditors to conduct a full financial and compliance audit each year. Therefore, your proposal would have a significant fiscal impact on each authority.

I thank you for the opportunity to comment on this report. Please contact me at 860.563.5851 should you have any questions.

Sincerely,

Emily C. Smith
Managing Director
Government & Corporate Relations