

STATE OF CONNECTICUT HEALTH AND EDUCATIONAL FACILITIES AUTHORITY

Audit-Finance Committee Special Meeting Minutes

January 13, 2021

The Audit-Finance Committee of the State of Connecticut Health and Educational Facilities Authority held a special telephonic meeting at 11:00 a.m. on Wednesday, January 13, 2021.¹

The special telephonic meeting was called to order by Mr. Mark Varholak, Committee Chair, at 11:00 a.m. and, upon roll call, those present and absent were as follows:

PRESENT: Peter W. Lisi, Board Chair
Mark Varholak, Committee Chair
Michael Angelini
Lawrence Davis
Darrell V. Hill

ALSO, PRESENT: Jeanette W. Weldon, Executive Director
Denise Aguilera, General Counsel
Debrah Galli, Manager, Administrative Services
Joshua Hurlock, Assistant Director, CHESLA
Daniel Kurowski, CHEFA CDC Program Manager
Carlee Levin, Senior Accountant
JoAnne Mackewicz, Controller
Michael F. Morris, Managing Director
Cynthia D. Peoples-H, Managing Director
Kara Stuart, Administrative Services Assistant of the Connecticut
Health and Educational Facilities Authority

GUESTS: Robert Smalley, Principal, BerryDunn
Katherine Balukas, Manager, BerryDunn
Richard Chirls, Tax Partner, Orrick/BLX Group
Sandra Stallings, COO, Managing Director, BLX Group
Ray Bentley, President, AMTEC Corp.

APPROVAL OF MINUTES

Mr. Varholak requested a motion to approve the minutes of the September 16, 2020 meeting of the Audit-Finance Committee. Mr. Hill moved for approval of the minutes, which was seconded by Mr. Lisi.

¹ All attendees participated in the meeting via conference telephone that permitted all parties to hear each other

Upon a voice vote, the “Ayes,” “Nays” and “Abstentions” were as follows:

AYES

Michael Angelini
Lawrence Davis
Darrell V. Hill
Peter W. Lisi
Mark Varholak

NAYS

None

ABSTENTIONS

None

Ms. Peoples introduced guests Katherine Balukas and Robert Smalley of BerryDunn, and Sandra Stallings and Richard Chirls of BLX Group.

BERRYDUNN – PRESENTATION OF INTERNAL AUDIT DRAFT REPORTS

CHESLA Scholarship Program

Mr. Smalley introduced Ms. Balukas who would be covering the two audits that were completed during the Summer of 2020.

Ms. Balukas stated that the first audit tested the CHESLA scholarship program while focusing on the scholarships that were awarded to individual students. The testing reviewed the policies and procedures as well as the testing of two student scholarships, one in the undergraduate program and one in the certificate program. The following criteria were used:

- Adherence to CHESLA’s procedures for awarding scholarships.
- In accordance with the eligibility criteria.
- Proper authorization from the scholarship committee.

Ms. Balukas reported that there were no findings or recommendations and CHESLA’s internal controls over the scholarship program are properly designed and were issued the highest rating of satisfactory.

CHESLA Vendor Oversight

Ms. Balukas stated that the second audit tested the oversight of outside vendors for the CHESLA loan programs. CHESLA has relationships with outside vendors who service and originate the In-School and Refi loans. Ms. Balukas stated that an important part of internal controls is overseeing the services that are provided by those outside vendors. The following criteria were used:

- Review user agreements for outside vendors of the CHESLA loan programs for identification of key terms and deliverables under the agreements.

- Review private and Refi loan program guidelines that are included in the user agreements.
- Review the System of Organization Controls (SOC) 1 Type 2 reports performed on the applicable outside vendors, including the available SOC 1 reports for subservice organizations.
- Review of an In-School loan and Refi loan originated for compliance with the program guidelines as documented in the user agreements.
- Review of payments made on an In-School loan and Refi loan made during the period.
- Review transition between outside vendors for origination and servicing of the refinanced loans.

Ms. Balukas reported that while CHESLA has a process in place to obtain SOC 1 Type 2 reports for the applicable third-party service organizations as well as other key deliverables as identified in the user agreements, it is recommended that CHESLA update their process to review and evaluate the complementary user controls identified in the reports to determine if these are incorporated into CHESLA's existing internal controls. CHESLA's internal controls over the oversight of outside vendors for the CHESLA loan programs were rated as adequate.

STATUS REPORT ON PRIOR CHEFA RECOMMENDATIONS

Ms. Balukas stated that a spreadsheet was created in order to track the status of prior recommendations from reports occurring over the last 2.5 years of engagement. Ms. Balukas reported that she worked with Ms. Peoples to categorize the recommendations into four main groups: client services, accounting, human resources and payroll, and information technology. Ms. Balukas stated that Ms. Peoples and the entire accounting team have done a good job working with the recommendations to incorporate changes to policies and procedures, and additional levels of review to strengthen the internal controls. There are a few recommendations that are still open in development including automation within the BONDS software and the ongoing general ledger. Regarding information technology recommendations, Ms. Balukas stated that Ms. Bode of BerryDunn, who originally performed the internal audit, will present the status of those items at the May meeting.

Regarding future internal audits, Ms. Balukas reported that in Summer of 2018 the original risk assessment had a three-year plan outlining the services BerryDunn would provide each year. Ms. Balukas stated the only item left open relates to the accounting function since the actual testing has been delayed given the general ledger conversion. Ms. Balukas stated that she and Ms. Peoples will begin working on the audit of these final items in April 2021. Ms. Balukas reported

that BerryDunn will then revisit their original risk assessment to determine if there are any significant changes to the risk levels or the frequency of audits that would need to be performed on those areas.

Mr. Varholak requested a motion to approve the internal audit draft reports from BerryDunn. Mr. Lisi moved for approval and Mr. Hill seconded the motion.

Upon a voice vote, the “Ayes,” “Nays” and “Abstentions” were as follows:

<u>AYES</u>	<u>NAYS</u>	<u>ABSTENTIONS</u>
Michael Angelini Lawrence Davis Darrell V. Hill Peter W. Lisi Mark Varholak	None	None

BLX GROUP – PRESENTATION OF INTERNAL AUDIT DRAFT REPORTS

Ms. Sandra Stallings and Mr. Richard Chirls of BLX Group introduced themselves. Ms. Stallings stated that BLX Group was engaged to provide consulting services related to CHEFA’s internal arbitrage reporting procedures and internal computations, as well as a review of the external arbitrage reporting prepared by a third-party vendor, AMTEC, for CHESLA. Ms. Stallings stated the following on the sampling size for the reports:

- CHEFA – of the more than 200 bond issues outstanding, selected a sample of 16 bond issues to review related arbitrage compliance documents
- CHESLA – of the 14 bond issues listed on the arbitrage summary, selected 2 Rebate Reports and 4 Loan Yield Reports to review for arbitrage compliance

Mr. Lisi inquired about the rationale behind the 16 bond issues that were selected. A brief discussion ensued.

CHEFA Arbitrage Procedures and Internal Reporting

Ms. Stallings reported the following on the overview of CHEFA procedures:

- Framed to reflect the current high level of experience of CHEFA staff
- Appears established procedures are being followed and supplemented with informal unwritten practices

- Procedures separated into 8 sections – new bond issues, spending exception, redemption, cash flows management, calculations, completed calculations and payment of liabilities, and templates
- Many bonds meeting a spending exception or considerable negative arbitrage. Overall non-compliance risk is medium to low given the negative arbitrage environment for most of the last decade.

Ms. Stallings reviewed the technical areas within the written procedures and reporting that need improvement.

Mr. Varholak inquired whether the procedures are being done, but there is just not a formal written procedure. Ms. Stallings stated that is correct, the procedures are being done, but there is not a formal written procedure documented.

Ms. Stallings stated BLX further reviewed areas in work paper documentation and informal procedures that should also be improved. A brief discussion ensued.

Ms. Stallings provided recommendations in the following related areas:

- Bond valuations
- Yield restriction compliance documentation
- Spending exception – alternative tax positions documentation
- Universal cap application
- Commingled reserve allocations and supporting workpapers
- Other areas of potential inaccurate reporting

Ms. Stallings reported that overall, CHEFA compliance with the arbitrage provisions in the procedures, as well as internal reporting were rated as adequate.

The floor was open to questions and a discussion ensued.

Ms. Stallings reported that management has agreed to review all items and take all the recommendations under advisement. Mr. Varholak inquired about the timeframe needed to reevaluate these items accurately for changes that have been made. Ms. Stallings stated that about 6 to 12 months is a feasible timeframe.

Mr. Varholak requested a motion to approve the CHEFA arbitrage procedures and internal reporting from BLX Group with the additional clarification that management will bring forth a high level plan to the May meeting remedying the findings that have been presented with an ultimate goal for things to be corrected within 6 to 12 months, with a follow up review by BLX.. Mr. Hill moved for approval and Mr. Angelini seconded the motion.

Upon a voice vote, the “Ayes,” “Nays” and “Abstentions” were as follows:

<u>AYES</u>	<u>NAYS</u>	<u>ABSTENTIONS</u>
Michael Angelini Lawrence Davis Darrell V. Hill Peter W. Lisi Mark Varholak	None	None

Ms. Balukas left the teleconference at 11:57 a.m.

Mr. Hill left the teleconference at 12:00 p.m.

CHESLA Arbitrage External Reporting

Ms. Stallings stated that BLX Group was engaged to provide a review of the external arbitrage reporting prepared by a third-party vendor, AMTEC, for CHESLA. The scope of work included the following:

- Review a sampling of the externally prepared (third party) arbitrage computations to be sure treasury regulations related to student loan financings are being properly applied on the rebate computations (non-purpose investments) or “Rebate Reports.”
- Review a sampling of the externally prepared (third party) arbitrage computations to be sure treasury regulations related to student loan financings are being properly applied on the loan yield computations (purpose investments) or “API Reports.”

Ms. Stallings stated that regarding the sampling size for CHESLA, of the 14 bond issues listed on the arbitrage summary, BLX Group selected 2 rebate reports and 4 loan yield reports to review for arbitrage compliance.

Ms. Stallings reported that BLX Group found that the following areas of the computations require increased regulatory guidance or additional technical analysis:

- Treatment of administrative expense offsets
- Application of universal cap
- Treatment of semi-annual gathering allowance.
- Consistency of bond yield calculations and usage.
- Consistency of bond year selection and usage.

Ms. Stallings reported that the level of risk for the CHESLA non-compliance with the arbitrage provisions was rated as high.

Ms. Stallings provided an overview on the material findings, significant findings, and minor findings for CHESLA. Ms. Stallings then provided an overview on the following recommendations:

- Accounting for the administrative expense offsets as determined under TR 1.148-5(e)(3) which allocates the allowable administrative bond related expenses over the weighted life of the portfolio as opposed to being allocated over the shorter computation period.
- Allocation of the universal cap to include the special definition of nonpurpose investments under TR 1.148-6(b)(2)(ii).
- Treatment of the semi-annual gathering allowance dates (5/15 and 11/15) to coincide with the debt service payment dates as required under TR 1.148-5(b)(1) and to only gather regular monthly loan payments.
- Consistent utilization (and compounding frequency) of bond yield between the rebate report and the API report for each bond issue in accordance with TR 1.148-4.
- Consistent use of bond year between rebate report and API report for a given bond issue in accordance with TR 1.148-1.

Ms. Stallings reported that overall, CHESLA external computational reporting was rated as needs improvement. A brief discussion ensued.

Ms. Weldon stated that some recommendations, e.g. those regarding the treatment of semi-annual gathering dates, have already been implemented. Ms. Weldon reported that CHESLA will be working with AMTEC to review the other recommendations and to take the appropriate steps for implementation moving forward. Ms. Weldon noted that in the past CHESLA's review of certain reports has been done as a team effort involving bond counsel and financial advisor. This

will be the approach going forward. Mr. Ray Bentley of AMTEC Corp. stated that AMTEC is open and supportive of taking a fresh look at approaches and implementing recommendations.

Mr. Varholak thanked Ms. Stallings and Mr. Chirls of BLX Group and Mr. Bentley of AMTEC Corp.

Mr. Varholak requested a motion to approve the CHESLA arbitrage external reporting from BLX Group with the additional clarification that management will bring forth a high level plan to the May meeting for remedying the findings that have been presented with an ultimate goal for things to be corrected within 6 to 12 months and to have a subsequent review by BLX. Mr. Lisi moved for approval and Mr. Davis seconded the motion.

Upon a voice vote, the “Ayes,” “Nays” and “Abstentions” were as follows:

<u>AYES</u>	<u>NAYS</u>	<u>ABSTENTIONS</u>
Michael Angelini Lawrence Davis Peter W. Lisi Mark Varholak	None	None

Mr. Varholak thanked management for the work they have done.

Ms. Galli left the teleconference at 12:17 p.m.

REVISED AUDIT-FINANCE COMMITTEE CHARTER

Ms. Aguilera stated that the proposed revision is to provide consistency to the charter. The charter currently requires an executive session with internal auditors but has no such requirement with regard to the independent auditors. Ms. Aguilera said the proposal is to remove the stated requirement to go into executive session with the internal auditors and noted that the committee always has discretion to go into executive session for appropriate reasons.

Mr. Varholak requested a motion to approve the revised audit-finance committee charter. Mr. Lisi moved for approval and Mr. Davis seconded the motion.

Upon a voice vote, the “Ayes,” “Nays” and “Abstentions” were as follows:

AYES

Michael Angelini
Lawrence Davis
Peter W. Lisi
Mark Varholak

NAYS

None

ABSTENTIONS

None

ADJOURNMENT

There being no further business, at 12:27 p.m., Mr. Lisi moved to adjourn the meeting and Mr. Angelini seconded the motion.

Upon a voice vote, the "Ayes," "Nays" and "Abstentions" were as follows:

AYES

Michael Angelini
Lawrence Davis
Peter W. Lisi
Mark Varholak

NAYS

None

ABSTENTIONS

None

Respectfully submitted,

Jeanette W. Weldon
Executive Director