

STATE OF CONNECTICUT HEALTH AND EDUCATIONAL FACILITIES
AUTHORITY

Minutes of
The Audit-Finance Committee Meeting
of May 20, 2008

The Audit-Finance Committee of the State of Connecticut Health and Educational Facilities Authority met in session on Tuesday, May 20, 2008.

The meeting was called to order by Benson R.Cohn, Chair, at 12:30 p.m. and, upon roll call, those present and absent were as follows:

PRESENT: Benson R. Cohn, Chair
John M. Biancamano
John Mengacci
Barbara Rubin

ABSENT: Howard G. Rifkin

ALSO PRESENT: Richard D. Gray, Executive Director
Jeffrey A. Asher, Managing Director/CFO
Cynthia D. Peoples, Assistant Director
Norberto Ramirez, Compliance/Internal Auditor
Eileen MacDonald, Manager, New Business/EasyLoan Program
JoAnne Mackewicz, Controller
Debra M. Pinney, Manager, Administrative Services
Peggy Root, Accountant
and Kathy Owens, Receptionist/Administrative Assistant, of
the Connecticut Health and Educational Facilities Authority

Guests: Catherine Dunne, Auditor, State Auditors of Public Accounts

The Notice of Meeting was read and ordered spread upon the Minutes of this Meeting and filed for the record.

The purpose of the Meeting is as follows: 1) Approval of Minutes of February 26, 2008; 2) Review of the Proposed FY 2009 Operating and Capital Budget; 3) Review Construction Fund/Wire Transfer Audit; 4) Presentation of FY 2009 Audit presentation; and 5) Conduct Executive Session.

Mr. Cohn requested a motion to accept the minutes of the February 26, 2008 Audit-Finance Committee Meeting. Mr. Mengacci made a motion to approve the minutes. Ms. Rubin seconded his motion.

Upon roll call, the “Ayes,” “Nays” and “Abstentions” were as follows:

AYES

John Mengacci
Barbara Rubin

NAYS

ABSTENTIONS

John Biancamano¹
Benson R. Cohn²

Mr. Colangelo arrived at 12:40 p.m.

Review of the Proposed FY 2009 Operating and Capital Budget

Before Mr. Asher presented the proposed budget, he introduced Ms. Catherine Dunne, from the State Auditors of Public Accounts, who is presently at the Authority conducting the audit for FY 2007. He stated that CHEFA received the approved copy of the audit for FY 2006, and the audit had no adjustments or recommendations, or findings.

¹ Mr. Biancamano was not present at the February 26, 2008 meeting.

² Mr. Cohn was not present at the February 26, 2008 meeting.

Mr. Asher referred to Page four of his memo stating that he will divide the presentation of the Capital and Operating Budget into three components. He stated that he will review compensation, new positions, proposed new space and an overview of the major changes. Ms. Mackewicz will discuss revenues and changes to the benefits budget, as well as any major components of the increase and operating expense budget and Ms. Peoples will discuss the IT Capital Budget and Arbitrage Rebate consultant.

Mr. Asher reported on the Compensation and Benefits section of the budget, as reported to the Human Resources Committee, the only major changes that Staff is proposing are the two new positions. The Compensation budget utilized the same methodology as FY 2008 for both merit increases as well as the employee incentive plan. The increase in compensation is a breakdown that was requested by the HR committee because they wanted to see how much of the increase in compensation was associated with current staff and the effect of the increase there; how much of the increase was associated with the annualized cost of those employees that were hired during FY 2008; and the cost of the compensation for the new staff that is proposed. With the estimated increase of compensation of \$324,000 there is a base salary, additional cost of \$188,000 of merit increases of approximately \$72,000; labor grade adjustments of \$19,000 and the concerning incentive compensation increase of approximately \$44,000. Mr. Asher referred to Page three of the memo concerning the merit increases and the methodology used which is the same as done previously, as well as the incentive. In addition, a breakdown was provided of incentives that were paid for the past three fiscal years. The increase of an average incentive is up to 9%. In FY 2007, CHEFA paid out \$178,000 and

that is broken down between costs associated with the Internal-Audit position which was added, incentive based on merit increases, labor grade adjustments, as well as two additional officers that are eligible for the 15% incentive. He also identified the components of the major increases in the budget which includes the new positions and some additional costs associated with the Business Continuity Plan. Although it is not a part of the capital budget, it is a change affected by IT and Ms. Peoples will explain that, a proposal of modification of our lease, additional costs associated with Arbitrage Rebate Calculations, and then budgeting the same amount for the Child Care interest rates subsidy.

As far as the two new positions, one is a carryover of the new position that was approved in the FY 2008 budget and staff is proposing to carry that position over to FY 2009. This person is going to provide support services to Mr. Morris in New Business, as well as to Mr. Wasch in the area of early childhood education. The second position is another Administrative Assistant position to report to Kimberley Fontaine to assist her in the administration of the Grants Program. We have 122 outstanding grants and more being added each time we award grants. This person will assist with the compliance monitoring that reports to the Legislature, going out to visit the facilities and assisting in the intake of the grants application which involves a significant amount of work. Both Mr. Asher and Mr. Gray believe that position is very well justified.

Mr. Biancamano asked what the Authority is doing now to accommodate with the workload of the Senior Financial Analyst. Mr. Asher replied that Mr. Morris has been

working an inordinate number of hours just to keep up with the workload. Ms. MacDonald has been participating to a great extent. Staff thought that the volume would taper off because of the auction rate conversions but there is still a significant amount of work.

In addition, Mr. Asher stated that he is concerned about the amount of work performed in the early childhood education area. The amount of work that Mr. Wasch is currently doing with the Early Childhood Education Cabinet and the Early Childhood Education Research and Policy Council, his involvement with the alliance and other work associated with the Demand Studies that are currently being done for SDE and the Legislature and the projected increases in the number of borrowers based on the additional debt service funding. We are currently working on Series G for child care and are in the process of receiving applications for Series H and we anticipate two or three series after that with the additional funding in the budget. Presently, we are at \$4.5 million in annual debt service appropriations and that number is scheduled to go up to \$8.5 million with a potential additional \$4 million in debt service appropriations. Mr. Asher indicated that that workload is going to increase significantly. Mr. Wasch will need assistance working on the additional bond issues as well.

Ms. Rubin asked if the Authority receives any revenue. Mr. Asher responded that for the additional bond issues, yes we receive revenues. We will get our annual basis points fees which is 9 basis points on the outstanding balance. CHEFA would earn an annual amount of \$36,000 per year for the \$40.0 million bond issue. Funding was transferred from the

State Department of Education to us to fund the Demand and Facilities Assessment Study and that money has been transferred over and we are working with consultants via an RFP to do that work as well. Mr. Wasch is supervising all of that work, as well as assisting the State Department of Education in preparing its report to the Legislature on the needs assessment in school readiness communities.

The expansion of the space is provided in more detail on Page nine of the Staff Memo. Staff approached CP Management, on behalf of the owner of the building at 10 Columbus Boulevard, looking at the possibility of expanding our office into this space which is a total of 2,525 square feet. The additional space is broken down into two spaces. There is approximately 1400 square feet behind CHEFA's office and the space across the hall equals approximately 900 square feet. When asked what their best offer would be, if CHEFA should decide to renegotiate the lease for another seven years. The building owner proposed effective August 1, 2008 to lower our lease from \$22 per square feet to \$20 per square feet and increase it by \$1 per year. Mr. Asher added that based on some numbers he had recently seen in Hartford on Class A office space the rate is around \$20.44 for Class A office space. This would save money on our current space. The building owner is proposing to give us \$50,500 in tenant improvement allowances and CHEFA would have to lease the full 2,525 square feet. Our proposal is to relocate the entire IT Department across the hall which would provide them with more secure work space. We had some conversation with Mr. Ramirez about this relocation and even though it is not mandatory, it is a best practice to have the IT Staff segregated from the rest of the Staff.

Since we have expanded into our current space, we have discovered that we do not have adequate additional break-out space for closings or other meetings. Therefore, we are proposing to expand so that we will have access from the Boardroom into the space behind the office to create additional conference space, as well as making it accessible from the main lobby area.

Mr. Asher stated that the major components of the increases in the budget are \$697,000 (\$324,000 compensation and benefits; \$150,000 arbitrage rebate; \$30,000 lease modifications; \$375,000 for interest rate subsidy on child care programs). We expect to use the additional interest rate subsidy. We have a couple of major loans that are on their way to closing.

Mr. Cohn asked if there were any questions or issues. Ms. Rubin recommended we should recognize how much of our budget is a donation to the community. A fair amount of this new space is a donation to the community. If a breakout room is used by others who are using our conference facilities and some portion of salary time is effectively donated to the community we should keep track of it. Running some of the Child Care Programs is on behalf of the State. It's not "our core business." There is a fair amount of contribution or charitable work that staff is doing.

Mr. Biancamano indicated that a 20% increase in expenses is a large increase. Ms. Rubin inquired if the \$324,000 for compensation includes the new positions. Mr. Asher

indicated that \$200,000 is for the existing staff. The current project actual compensation actual base for FY 2008 is \$1,975,000.

Dr. Cibes joined the meeting at 12:50 p.m.

Ms. Rubin indicated that a fair amount of our increase over the years is giving away our services to third parties. We should just acknowledge this and track it.

Mr. Colangelo inquired if we were not giving away those resources, what would be happening with those funds? The Committee agreed that the funds would most likely be given away in Grants.

Ms. Rubin is concerned that we are taking a liability that has a more permanent nature. For example, if you enter into a lease and your business cuts back, that lease still is in effect for seven years.

Ms. Mackewicz reported for FY 2009 CHEFA is projecting a bottom line of \$896,000; revenue projection is \$6.3 million; which is an increase of \$11.9% over FY 2008. That includes our current outstanding and also includes \$442,000 from the deals that we intend to close which are approximately 12 new deals or \$578,000. We have included about \$781,000 in investment income which is a little less than FY 2008 because we are predicting a decrease in yields to 3.5%.

Ms. Mackewicz stated the other lines items have not changed significantly in the benefits area other than compensation itself. The life insurance and the pension increased relative to the increase in compensation. The HSA medical insurance that CHEFA switched to in January 2008, we are also planning to keep in place. It was a high deductible plan that CHEFA chose to fund. This resulted in a savings of approximately \$151,000. This includes an 11% increase in January 2009 and it also includes the two new staff positions at the more conservative rate which is the higher rate, if they chose the family and each of their \$4,000 HSA funding. Tuition also increased; there is three new staff that will be entering into a graduate programs. On the operations side, the business insurance we have is not expected to increase at all based on our usage rates. We have not used any of those insurances. In FY 2008 the usage of the copier increased so we increased the budget for that item.

Staff education is broken down into three different categories; collectively they are increasing by approximately \$4,000 which is primarily due to Arbitrage training, as well as some technical IT training. Consultants/others are increasing due to Arbitrage which Ms. Peoples will explain. Ms. Mackewicz asked if there were any questions.

Ms. Rubin inquired as to how much of the new issuance relates to incentive compensation and asked if this is a stretch goal, or why do we have it in the incentive compensation component if we know it is already going to come through.

Mr. Asher responded that we can't go out and market our business. Ms. Rubin suggested taking it out of incentive comp. Mr. Asher replied that we really have no control over it. We discussed focusing on incentive compensation more on expenses being over or under-budget not focusing on the bottom line; we agreed to pull that out last year. Mr. Gray stated that it is an expense-based control plus net revenue. He added that we do not base it on income anymore. Mr. Asher stated that we are sure of these projections based on conversations we have had with all our institutions. Ms. Rubin inquired if the Authority receives unexpected new business. Mr. Asher replied that we do but added that we control expenses; we do not have any control over the revenue or investment income. Ms. Rubin responded that CHEFA does market its services when they go to schools and speak to them about what CHEFA can do for them. Mr. Asher replied that CHEFA cannot encourage any institution to issue debt. Mr. Asher stated that we are here to provide a service to the institution and he believes that we would be violating the spirit of what we are supposed to be doing by encouraging people to accelerate their closings. Further discussion ensued.

Mr. Cohn asked if there were further questions. There being none, he turned the floor over to Ms. Peoples.

Ms. Peoples first reported on the two larger items impacting the operating expense budget. Business Continuity increased by approximately \$12,000 due to a proposal to move the equipment in Albany to another location. The current facility has had power issues and internet issues. They have not been available when we needed them to be to

get access to our equipment. We received three quotes to provide us with better service including full redundancy for power and network. The equipment cabinets would be secure and locked. We would have 24 hour access to the facility requiring biometrics and key cards.

The other item on the expense side is the Arbitrage Rebate Calculation Services. The person performing the calculations left for another position. What we are proposing to do for a period of the year is to send out the calculations to a rebate shop to perform the calculations for us. We've estimated about 30 calculations at \$5000 for a total of \$150,000 for the calendar year.

Ms. Rubin asked if the person is included in the budget. Ms. Peoples responded affirmatively. Ms. Peoples explained that presently we have a person who is assisting with the process of performing the calculations. She is assisting with gathering the information and putting it together so that we can outsource it. Ms. Peoples added that she is qualified, pending training for specific calculations. The idea was to bring someone in who is a temporary employee who could possibly fill the position. She has learned some components of it. The idea is to continue to outsource and if that does not work, to hire someone late summer.

Mr. Asher stated both are in the budget but the issue is that we have a requirement that we have to keep up with these calculations and they have to be done on a timely basis. We have had a significant increase in the number of calculations we have had to do because

of an increase in bond issues that is why we need to do both. Mr. Cohn asked if there were any plans to have the outside person to check and make sure the temporary employee is performing the calculations correctly. Mr. Asher and Ms. Peoples responded affirmatively.

Ms. Rubin asked if there would be a savings of the \$150,000 if the person learned the job more quickly. Ms. Peoples explained that arbitrage rebate is very complicated. It took the previous employee approximately 2 ½ years into calculations and they found there were still things they could improve upon. Ms. Peoples added that she does not expect in six months the temp would be able to perform calculations without outside help.

Mr. Gray reiterated that this is mandatory and represents an enormous potential liability if not performed correctly. Our clients could lose hundreds or thousands of dollars in arbitrage earnings. Dr. Cibes asked if it would be less expensive to outsource all of the calculations. Ms. Peoples responded that it would be more expensive because it would cost approximately two salaries, if not three.

There being no further questions or discussion, Ms. Peoples proceeded to the Capital Budget. She indicated that CHEFA would like to add a wireless network into the Conference Center. We would like to continue with our 3 year desktop replacement plan; one laptop needs to be upgraded; a 48-port network switch for office expansion; battery back-up for the expansion and in support for phase 1 and 2 server virtualization project; carryover for the HP5si replacement; for the VoIP phone system we are proposing a

conference phone to use in other conference space on the software side, Visual Studio 2 licenses, SQL Server 2008 upgrade from SQL 2000. Leasehold improvements include an electrical ground for the telephone system; wiring for the new battery back up – 240 volt, and a fail over A/C for the IT room. Due to a recent failure of the A/C in the IT room and subsequent equipment failure we felt it necessary to install a back up.

Mr. Colangelo asked how much CHEFA's Capital Budget was last year. Ms. Peoples responded that it was \$72,500 and we spent most of it with the exception of approximately \$5,000 to \$7,000, which will be spent by the end of this fiscal year.

Office expansion is approximately \$76,000 that includes: construction, wiring, equipment, furniture and fixtures, etc. Ms. Peoples stated for the server virtualization this would be the first opportunity we have had to restructure the architecture of our network systems. Our prior plan outlined when we would purchase new equipment and how we would redeploy the older equipment. In the process, we have outgrown the capacity of some of our servers and added additional service load to our servers which could cause problems. We want to bring in "controllers" for our network which will assist with "load balancing". Ms. Peoples further explained the benefits of server virtualization.

Mr. Gray added that Ms. Peoples and her team have been utilizing the servers as best as they can over the last few years. He recommended that it is time to have the outdated equipment replaced.

Ms. Rubin asked if we will need to allocate more funds for the future years. Ms. Peoples responded that it will be more discretionary as to what needs to be replaced or updated.

Mr. Cohn asked if there were further questions. Ms. Rubin asked how much is in the Grant Program budget. Mr. Asher responded that \$550,000 is budgeted for each of the Grant Programs, the same as last year.

Mr. Cohn requested a motion to approve the Operating and Capital Budget for FY 2009.

Mr. Colangelo moved; Ms. Rubin seconded his motion; all were in favor.

Upon roll call, the “Ayes,” “Nays” and “Abstentions” were as follows:

AYES

NAYS

ABSTENTIONS

John Biancamano
Benson R. Cohn
Patrick A. Colangelo
John Mengacci

Construction Fund/Wire Transfer Audit – Mr. Ramirez

Mr. Ramirez reported that he completed the Construction Fund/Wire Transfer audit and thanked Ms. Mackewicz, Ms. Root and the entire Accounting Department for their diligence in organizing material for the audit. He stated that, overall, the internal controls and procedures for the Construction Fund and Wire Transfers functions are reasonably adequate. There were four minor findings and recommendations were made to improve those areas.

The first finding is the primary administrators of one of the wire systems did not comply with two of the entitlements they are responsible for: 1) Add, modify or delete application users; and 2) Perform digital certificate maintenance. It is very important to add new employees after the first 30 days of employment. If an employee retires or is terminated, they should be removed from the system immediately. The digital certificate is used to identify the computer where the wire transfers are done. For example, Mr. Gray cannot perform a wire transfer from Mr. Asher's computer because he has his own password and certificate. In addition, Management failed to provide maintenance to the certificates. If certificates are not used in 30 days, they can become obsolete.

Mr. Ramirez made a recommendation to the Accounting Department to establish proper controls in order to make sure that all the entitlements listed on the wire system agreement are executed on a timely basis. In addition, Officers should perform wire transfers once a month in order to keep the certificate updated. Mr. Ramirez added that he also asked Ms. Mackewicz to let him know when passwords were being changed in order to verify that both wire systems are working properly.

Mr. Ramirez reported that 23 project fund requisitions of reimbursement were reviewed from 13 different institutions issuing bonds during FY 2007. The following findings were noted: One out of 23 requisitions was not properly reimbursed resulting in an inappropriate payment of \$2,187. The Accounting Department already recouped the overpayment with the subsequent requisition.

The Authority's process for project expense reimbursement lacks proper segregation of duties. It is the Authority's practices to have an Officer approve the project expense packages while the same Officer is also allowed to approve the release of the final payment by wire transfer.

Mr. Asher added that it is difficult because we have a limited number of people that are authorized to release wire transfers and a significant number of projects are overseen by Mr. Morris. Mr. Asher also stated that he authorizes for release approximately 95% of wires. We need to get other Officers to perform more wires which would keep them up-to-date.

Mr. Ramirez responded that the main issue is that we were relying on Mr. Morris and Mr. Asher to perform all the wires. The CIAF recommends to the accounting Department to design a system in which the Officer authorizing the reimbursement of the project expense package is not the same Officer approving the release of the wire. The Accounting Department has adjusted the procedures to require a different releasing Officer, from the approver of the reimbursement package. In addition, two additional Officers have been established.

Mr. Ramirez reported that the Policies and Procedures for Construction Fund and Wire Transfer disbursements included in the Authority's Policies and Procedures Manual do not reflect the current practices applied by the Authority Staff. In addition, the Authority

did not have written procedures for recover/system failure, rejected transactions and incoming wires.

The CIAF recommended to the Accounting Department to review Section 5.1.3 Construction, Cost of Issuance and Capitalized Interest Account Disbursements of the Authority's Policies and Procedures Manual at least every two years in order to include updates, improvements and new controls. In addition, the CIAF also recommended to the Accounting Department to establish written procedures for the recovery/system failures; rejected transactions; and Incoming wires. Management agrees and will update the Policies and Procedures periodically as changes occur a minimum of every two years.

Finally, twelve incoming wires were reviewed for FY 2007. CIAF found that the form used by the Authority Staff as a backup support for transfers between CHEFA accounts lacks the necessary data to create an adequate and reasonable trail of separation of duties.

The CIAF recommended to the Accounting Department redesign the form used as a backup support for transfers between accounts in order to have in place a valid form that constitutes a good audit trail.

The form has been redesigned. This form clearly defines the purposes, fund to account, fund from account, requester, and a newly added line for the approver and releaser with corresponding signatures. Accounting has also established a binder to retain all wire transfers between funds that are not construction fund related.

Mr. Cohn asked if there were any questions regarding the Construction Fund/Wire Transfer Audit. There being none, Mr. Cohn requested a motion to accept the Construction Fund/Wire Transfer Audit Report. Mr. Mengacci moved to accept the report; Mr. Biancamano seconded his motion.

Upon roll call, the “Ayes,” “Nays” and “Abstentions” were as follows:

AYES

NAYS

ABSTENTIONS

John Biancamano
Benson R. Cohn
Patrick A. Colangelo
John Mengacci

FY 2009 Audit Plan presentation – Mr. Ramirez

Mr. Ramirez presented to the Committee the FY 2009 Proposed Audit Plan. He stated that the following factors were considered in determining the risk of the auditable areas. CIAF reviewed changes/new risks in the audit universe; we also considered the financial, legal, political and strategic risks; external and internal audit results; and other environmental factors, such as changes in personnel and operations, future business strategies, management’s concerns, and major changes in operations, programs or systems.

Mr. Ramirez also performed an analysis of audit and administrative hours in order to better budget for the next year.

Risk Assessment

This year it was decided to use the same assessment performed in FY 2007 since no major changes occurred. The assessment was updated through interviews and questionnaires in order to update each area. Interviews were conducted with each Manager, the Executive Director and the CFO. CIAF also conducted interviews and questionnaires with new employees and/or individuals assigned to new responsibilities.

CIAF validated the audit universe and risk universe; prioritized audit areas and draft plan and review /approval of Audit-Finance Committee for the FY 2009 Audit Plan.

Risk Map

Mr. Ramirez explained on the Risk Map and identified the critical risks that potentially threaten the achievement of business objectives and this quadrant is empty because CHEFA does not have any high risk areas. The orange quadrant is the Medium Risk Area (lower likelihood, but could have significant adverse impact on business objectives). The areas that fell within this quadrant are Child Care; Internal Control System; Reinvestment/Arbitrage; Construction Fund/Wire Transfer; Business Continuity Plan; EasyLoan/EasyLease; Compliance System; Payroll/Personnel; CHEFA State Ethics Policies; Accounting System and IT function.

The blue quadrant or the Low Risk quadrant (significant monitoring not necessary unless change in classification; periodically reassess) includes Grants; Child Care (SD); customer satisfaction; and CHEFA fees.

The last quadrant is the yellow quadrant which represents areas with lesser significance, but more likely to occur. The only area that fell in this quadrant is the B.O.N.D.S. System.

Mr. Ramirez then presented an analysis of the hours that have been charged by the Compliance Internal Auditor.

Mr. Ramirez reported that as of May 12, 2008, he has charged 1,808 hours as follows: audit hours – 1,260 and indirect hours – 548; for a 70% and 30%, respectively.

Mr. Ramirez then presented a breakdown of the audit and indirect hours, including the hours charged on the three completed audits as of May 2008.

Mr. Ramirez shared with the Audit-Finance Committee the FY 2009 Audit Plan and Budget. He explained that five (5) areas were selected for the upcoming year. These areas are Business Continuity Plan; B.O.N.D.S. System; Payroll/Personnel/Ethics; Reinvestment/Arbitrage; and the Internal Control System which is part of each individual audit.

Mr. Ramirez also explained two alternative areas were selected: Accounting System (automation) and Easyloan/Easylease. These two areas will be audited only if time permits.

Finally, Mr. Ramirez discussed the FY 2009 Compliance Internal Audit Budget with Audit-Finance Committee. He explained that the increase over the last year is due to two new educational items: Graduate Certificate in Public Financial Management and the CIA (Certified Internal Auditor) exams.

Mr. Ramirez asked the Audit-Finance Committee for approval of the FY2009 Audit Plan.

Mr. Cohn asked if there were any questions or comments concerning the Compliance/ Internal Audit Plan. There being none, Mr. Cohn requested a motion to approve the FY 2009 Audit Plan presentation. Ms. Rubin moved to approve the Audit Plan; Mr. Biancamano seconded her motion.

Upon roll call, the “Ayes,” “Nays” and “Abstentions” were as follows:

AYES

NAYS

ABSTENTIONS

John Biancamano
Benson R. Cohn
Patrick A. Colangelo
John Mengacci

The Committee agreed that there was no need to conduct an Executive Session. The meeting was adjourned at 1:50 p.m.

Respectfully submitted,

Benson R. Cohn, Chair

Audit-Finance Committee