

**Colorado Health Benefit Exchange
Report to the Finance Committee
Regarding the June 30, 2016 Audit**

• **Highlights of the Financial Statements for the Year Ended June 30, 2016:**

- Financial statements are comparative with unmodified (i.e. “clean”) opinion for 2016. A Single Audit was required for 2016. We had “going concern” discussions with management to determine the financial viability of the Exchange through June 30, 2017.

Statements of Net Position:

- Cash had a balance of \$12,745,709 at June 30, 2016 compared to \$33,741,071 at June 30, 2015.
- Accounts receivable totaled \$12,774,535 at June 30, 2016 compared to \$6,136,214 last year, an increase of \$6,638,321. Accounts receivable consist mainly of amounts due from carriers for fees earned, for which rates assessed increased for fiscal 2016 (see below).
- Capital assets have a net book balance of \$30,854,999 at June 30, 2016 compared to \$37,241,086 at June 30, 2015, and consist mostly of software and web portal development. Capital assets purchased during the year ended June 30, 2016 totaled \$6,185,263, compared to \$12,951,637 last year. Depreciation and amortization expense was \$12,571,350 for 2016 and \$9,519,628 for 2015.
- Accounts payable and accrued liabilities totaled \$3,931,822 at June 30, 2016 versus \$8,130,577 at June 30, 2015. The decrease of \$4,198,755 is due to the winding down of large technology contracts and development of the Exchange.
- Unearned revenue totaled \$47,874 at June 30, 2016, compared to \$5,161,429 at June 30, 2015. At June 30, 2015, a net liability of \$5,120,886 had been recognized under unearned revenue for amounts due under the federal grant. The Exchange made certain corrections to the federal grant for unallowable costs identified subsequent to year-end and time of payment, resulting in the overdrawn grant balance at year-end. This balance was spent down during fiscal 2016.
- Net position totaled \$56,208,273 at June 30, 2016. Of this amount, \$30,854,999 is invested in capital assets, and \$183,750 is restricted by a grant for spending on a specific purpose, leaving an unrestricted balance of \$25,169,524.

Statements of Revenues, Expenses, and Changes in Net Position:

- For 2016, the Exchange had a (\$13,326,051) decrease in its net position compared to a \$14,110,963 increase in 2015. After eliminating depreciation, there is a (\$754,701) decrease in net position for 2016 versus a \$23,630,591 increase in 2015.
- Federal grants revenue totaled \$5,346,702 for 2016 compared to \$45,815,793 for 2015, and consists of revenue from the Level 2 grant, under the State Planning and Establishment Grants for the Affordable Health Care Act (ACA)’s Exchanges. This grant expired June 30, 2016 and all remaining amounts were fully drawn on the grant during fiscal 2016.

**Colorado Health Benefit Exchange
Report to the Finance Committee, Continued
Regarding the June 30, 2016 Audit**

- Program revenue totaled \$22,178,323 for 2016, compared to \$26,398,708 for 2015, and consists of revenue mandated under HB 13-1245. Under HB 13-1245, a fee was assessed on carriers at \$1.80 per number of lives covered per month for calendar 2016 and \$1.25 per number of lives covered per month for calendar 2015. This fee is only allowed to be assessed through December 31, 2016. The Exchange did not receive any disbursements from the unclaimed property trust fund during 2016, but received \$14,035,553 in 2015. The Exchange also received tax credit contributions from carriers totaling \$5,000,000 in both 2016 and 2015.
 - Fees for service revenue totaled \$14,664,752 for 2016, compared to \$6,863,548 for 2015. This revenue consists of a fee assessed on carriers totaling 3.5% for each policy sold during calendar year 2016 and was 1.4% for each policy sold in calendar 2015.
 - Expenses totaled \$58,712,350 and \$68,065,291 for 2016 and 2015, respectively, a decrease of \$9,352,941. Decreases were seen in most expense areas in an effort to cut costs. Salaries, payroll taxes, and benefits expenses increased by \$2,028,623 in an effort to increase the personnel employed by the Exchange and use fewer outside contractors.
- **Single Audit Reports**
 - The OMB Uniform Grant Guidance was issued December 2013 and applies to federal grants entered into after December 26, 2014. Because the Exchange's federal grant was issued prior to this date, the new guidance did not affect the Single Audit of the Exchange. However, Subpart F, which relates to audit requirements of Single Audits, applies to audits of fiscal years beginning on or after December 26, 2014. Therefore, the audit requirements were implemented for the Exchange with the current audit.
 - **Operational Matters Letter** – See Attachment
 - **Communication with Those Charged with Governance** – See Attachment
 - **Other Matters**
 - Subsequent events update.
 - The tax return is being prepared by KCE and is due February 15, 2017.
 - **Acceptance of Financial Statements**
 - **Executive Session with the Auditors**

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12/19/2016

**Colorado Health Benefit Exchange
(dba Connect for Health Colorado)**

**Financial Statements and Required Supplementary
Information**

June 30, 2016 and 2015

(With Independent Auditor's Report Thereon)

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Colorado Health Benefit Exchange

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Single Audit Reports

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Independent Auditor's Report

**Board of Directors
Colorado Health Benefit Exchange:**

Report on the Financial Statements

We have audited the accompanying financial statements of Colorado Health Benefit Exchange (the Exchange), as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Colorado Health Benefit Exchange as of June 30, 2016 and 2015, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Directors
Colorado Health Benefit Exchange

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3-7 be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2, *U.S. Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 19, 2016, on our consideration of the Exchange's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Exchange's internal control over financial reporting and compliance.

January 9, 2017

Management's Discussion and Analysis

Colorado Health Benefit Exchange Overview

In 2011, the Colorado General Assembly passed Senate Bill 11-200, which created the Colorado Health Benefit Exchange, now doing business as Connect for Health Colorado (C4HCO), as a public non-profit entity governed by a Board of Directors and reviewed by the Legislative Health Benefit Exchange Implementation Review Committee. The organization's mission is to increase access, affordability and choice for individuals and small employers purchasing health insurance in Colorado. C4HCO is intended to reflect the unique needs of the state, seek Colorado-specific solutions, and to support an open competitive marketplace. C4HCO is serving the individual and small group markets, with an initial potential customer base of one million Coloradans.

The number of Coloradans selecting a medical plan through the individual Marketplace increased by 28% from 153,000 in plan year 2015 to 196,000 for plan year 2016 (through September). Coloradans from every county in our state signed up for medical coverage through the Marketplace. Additionally, as of June 2016, 384 small businesses provided coverage to 2,880 employees through enrollment in the SHOP program. For 2016 plans, C4HCO helped return \$231 million through September 2016 to Coloradans through Advance Premium Tax Credits and Cost Sharing Reductions. Over seventy percent of our customers in 2016 qualified for this valuable financial assistance.

Connect for Health Colorado completed a series of significant technological, organizational advancements and transitions in fiscal year 2016 to set the foundation for long-term success and sustainability. The third open enrollment period faced challenges initially with the discontinuance of the Colorado HealthOp as one of the major plans on the exchange. Two weeks before open enrollment, Connect for Health Colorado made major system changes, including recalculating tax credits, re-running renewal data and notifications, and removing HealthOP plans from the marketplace. Despite this challenge, the third open enrollment period resulted in increased year over year enrollment. Connect for Health Colorado gathered feedback from stakeholders and partners and used that information to guide preparations for the 2017 plan year open enrollment period. Throughout the year, the organization improved all levels of operations, guided by three priorities:

- Optimize the customer experience
- Stabilize and right-size staffing, systems and processes
- Put the Marketplace on the path to long-term financial sustainability.

Operationally, the organization has taken steps during fiscal year 2016 to reduce expenditures in the transition from being funded by federal grants to being funded by earned revenue. These reductions resulted from placing the Customer Service Center under a single vendor with tighter controls on cost fluctuations, a reduction in the scope of the assistance network, reducing and focusing marketing spending, and the renegotiation of technology maintenance and operations costs.

Connect for Health Colorado adjusted to leadership transition, staff turnover, planned growth, audits and strengthened fiscal management. The Finance and Operations Committee, Board of Directors and the Colorado Health Insurance Exchange Oversight Committee provided continuous guidance, reviewing the FY2017 budget in June 2016. The FY 2017 budget includes strategies to further reduce vendor costs, modify the organizational staffing structure and increase enrollment.

Funding

In June 2013, Colorado's Governor signed HB 13-1245 into law, which in conjunction with administrative fees charged for policies purchased on the Marketplace, supports C4HCO becoming a self-sustaining entity after the end of the federal grant period. More specifically HB 13-1245 allowed for C4HCO to collect a broad market assessment on medical and dental policies in the small group and individual markets sold between 2014 and 2016. For 2015, the Board voted to set the fee at \$1.25. For 2016 the fee was set at \$1.80.

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Beginning on January 1, 2014, C4HCO charged administrative fees on all policies sold through the Marketplace. The Board will continue to set the fee on an annual basis considering such factors as annual budget requirements, technology and operational reserves, average premiums and enrollment projections. The Board set the fee for calendar years 2014 through 2016 at 1.4%, 1.4% and 3.5%, respectively. The increases in both the administrative fee and the broad market assessment should provide for a smooth transition from the use of Federal grants for ongoing operational purposes and contribute to the long-term sustainability of the organization.

Fiscal year 2016 was the final year to receive Federal grant funding. Three Federal grants have been awarded by the Department of Health and Human Services since the inception of the organization.

- First Level 1 Establishment Grant, \$17,951,000, awarded February 22, 2012, and closed out in 2013.
- Second Level 1 Establishment Grant, \$43,486,747, awarded September 27, 2012, and closed out in April, 2014.
- Level 2 Establishment Grant, \$122,301,350, awarded July 9, 2013 and initially scheduled to close December 31, 2014, additional no cost extensions have been granted through June 30, 2016.

One requirement of the Level 2 grant was to develop a sustainability plan that would ensure the ongoing operations of the Marketplace after federal funding ends. Through the steps taken in increasing the administrative fee and broad market assessment, stabilization of the technology, along with tighter cost controls and the pursuit of Medicaid cost sharing, C4HCO is actively implementing its sustainability plan.

Financial Statements

C4HCO's financial statements are prepared in accordance with accounting principles generally accepted in the United States as promulgated by the Governmental Standards Accounting Board (GASB). The Statements of Net Position; Revenues, Expenses, and Changes in Net Position; and Cash Flows are prepared on an accrual basis, and combined with the notes to the financial statements, provide the reader with an overview of the financial position and activities of the organization.

Fiscal year 2016 showed a significant decrease in the proportion of our funding coming from federal grants from 56% in fiscal year 2015 to 12% of total revenue. The primary sources of funding replacing federal grant funds came from the broad market assessment and administrative fees on plans purchased on the exchange.

Total assets decreased between 2015 and 2016 by \$22.5M (\$60.5M compared to \$83.0M). Contributing to this decrease, long-term assets decreased by \$8M (\$32.3M compared to \$40.3M) consisting of the net impact of capital investments totaling \$6.2M offset by \$12.6M of depreciation and amortization charges. Capital investments primarily focused on technology enhancements to the exchange software and integration with the States eligibility system. Also contributing to the overall decrease in total assets, was the decrease in current assets of \$14.5M (\$28.2M compared to \$42.8M). This decrease primarily consisted of a decline in cash balances of \$21M (\$12.7M compared to \$33.7M) offset by a \$6.6M increase in receivable balances. Changes in cash are included in the discussion of the Statements of Cash Flows. The increase in receivables resulted from higher levels of program and service fees at the end of the fiscal year as discussed in the operating revenue section below.

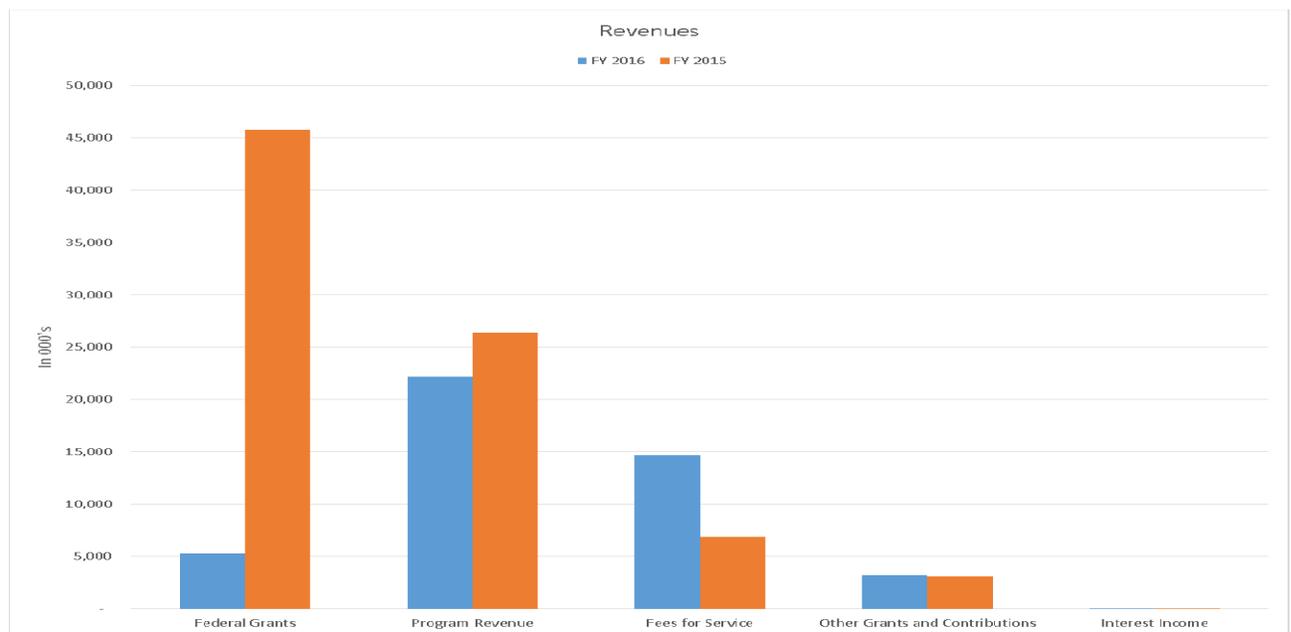
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The change in liabilities between 2015 and 2016 of \$9.2M (\$4.3M compared to \$13.5M) consists primarily of a decrease of \$3.9M in accounts payable (\$3.7M compared to \$7.6M) and a decrease in unearned revenue of \$5.1M (\$0 compared to \$5.1M). Payable decreases resulted from the timing and overall lower level of infrastructure expenditures between the two years. The decrease in unearned revenue was the result of federal grant payments received in the prior year but applicable to current year expenditures.

The difference between assets and liabilities represents the net position of the organization, and the change in net position over time is one indicator of the organization's improving or declining financial position. As expected in fiscal year 2016, due to the close out in federal funding and the completion of major infrastructure enhancements, the net position of the organization decreased by \$13.3M. The decrease in net position is reduced to (\$0.8M) when the impact of depreciation and amortization expense (\$12.6M) is taken into account.

Operating Revenues

Total revenues for the fiscal year decreased by \$36.8M or 45% (\$45.4M compared to \$82.2M) from the prior year.



Total federal grant revenue for the year was \$5.3M which was a decrease in federal grant revenue of \$40.5M or 88% (\$5.3M compared to \$45.8M) from the prior year. The decrease was in line with budget expectations of the grant closing in fiscal year 2016. All federal funds were expended by June 2016.

During Fiscal Year 2016, C4HCO generated \$22.2M in program revenue. Program revenue consisted of \$5.0M from carrier tax credits and \$17.2M from special fee assessments. The special fee assessment increased by \$9.8M or 132% (\$17.2M compared to \$7.4) from the prior year due to an increase in the fee structure effective January 2016. Overall, program revenue decreased year-over-year by 16% or \$4.2M due to \$14.0M in one-time revenue from CoverColorado recorded in fiscal year 2015.

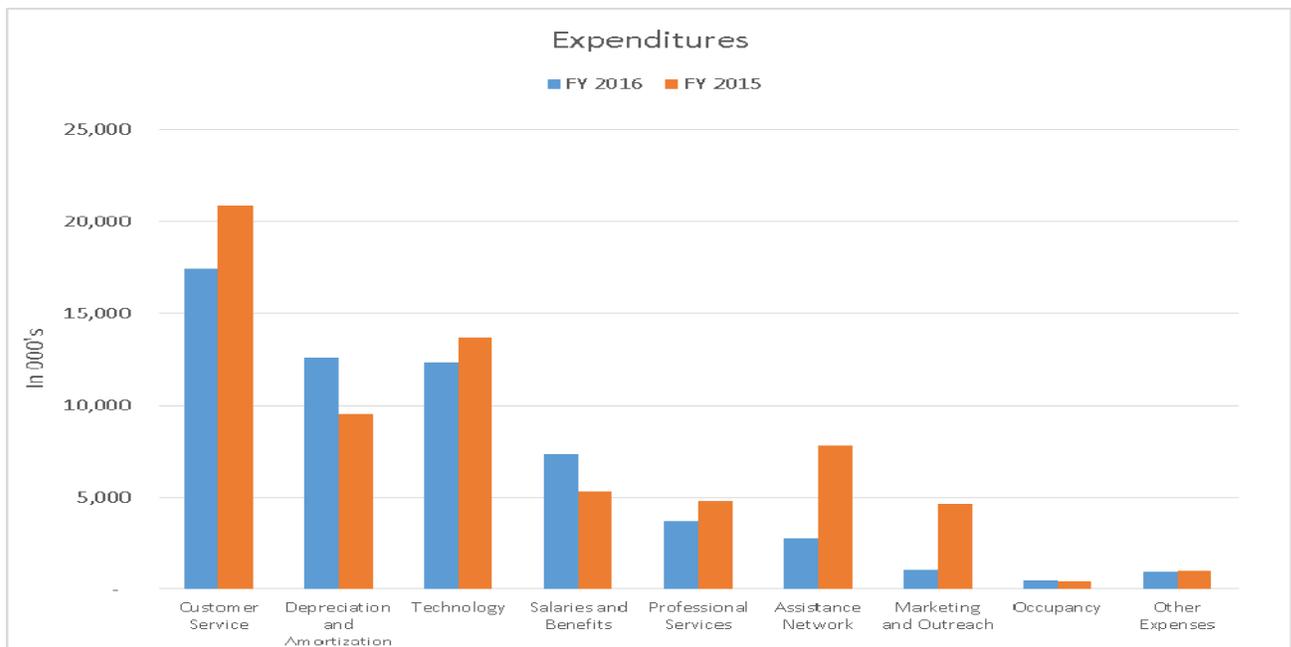
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The fees for service revenue increased by \$7.8M or 114% (\$14.7M compared to \$6.9M). The increase in fees for service were due to an increase in enrollments through the exchange along with an increase in the fee structure in January 2016.

Other revenue recorded in 2016 included non-federal grants totaling \$3.1M and interest income of \$22,950.

Operating Expenditures

Total expenses for the fiscal year decreased by \$9.4M or 14% (\$58.7M compared to \$68.1M) from the prior year. Removing the impact of the change in depreciation and amortization, expenses decreased by \$23.4M, or 21%, from the prior year.



Some of the more significant changes in expenditures included:

- Customer service expenses decreased by \$3.4M or 16% (\$17.4M compared to \$20.8M) as the result of a procurement of a new vendor and more favorable contract terms.
- Technology expenses decreased by \$1.3M or 10% (\$12.4M compared to \$13.7M), primarily due to a lower level of overall system changes resulting from a maturing of the shopping platform.
- Depreciation expense increased by \$3.1M or 32%, which is directly related to capital assets placed in service from inception-to-date. The majority of capital assets will become fully depreciated by fiscal year 2018.
- Salaries increased by \$2.0M or 38% (\$7.3M compared to \$5.3M) due to the movement away from the use of contractors.
- Assistance network costs decreased by \$5.0M or 65% (\$2.8M compared to \$7.8M). This decrease reflected the stabilization of the assistance network to a sustainable level following the initial start-up funded by the federal grant.
- Marketing and outreach decreased by \$3.6M or 77% (\$1.1M compared to \$4.7M) from the prior year. The utilization of grant funds in fiscal years prior to 2016, was primarily used to build a sustainability “baseline” for the organizations statewide marketing framework. This framework aided in gaining operating efficiencies and streamlining and focusing marketing costs in FY16.

Statements of Cash Flows

The Statements of Cash Flows represent C4HCO's change in cash and cash equivalents for the year and provides a summary of how cash was utilized. Cash balances decreased by \$21.0M or 62% (\$12.7M compared to \$33.7M) in fiscal year 2016. As reflected in the statements of cash flows, \$14.8M of cash was used for operating activities during the year compared to \$25.5M generated by operating activities in the prior year. This change was primarily the result of winding down the federal grant in the current fiscal year resulting in a \$60.2M drop in cash drawn on the grant over the prior year. In addition, in the prior year a one-time payment of \$14M was received from the expiring CoverColorado program. Partially offsetting the lower revenues received in the current fiscal year were lower operating costs due to the maturing of the technology infrastructure and reduced customer service costs. Capital expenditures also dropped from the prior year by \$6.2M offsetting further the cash impact of the drop in federal funding.

Currently Known Facts and Conditions

Connect for Health Colorado continues to operate in an environment of change and growth. As the result of recent elections this environment of change is expected to continue. While the future of the Accountable Care Act is uncertain at the time of this report, the foundational mission of the exchange as originally envisioned by the state remains the same. With an eye to the future, C4HCO continues with its plans for sustainability. This plan focuses on the growth of enrollment combined with the management of operational costs. Since the end of the fiscal year the organization has made great strides in further reducing recurring technology expenditures. With modest growth in enrollment based revenue over the next three years combined with modest cost reductions, the organization is on a path to financial sustainability.

C4HCO mission is to increase access, affordability, and choice for individuals and small employers purchasing health insurance in Colorado. Enrollment is a key metric used to measure the success of the organization and the achievement of its mission. For the current open enrollment period, which began November 1, 2016, a special focus has been placed on Coloradans that are eligible for insurance subsidies under the Accountable Care Act but who are not enrolled in a plan. While still early in the current open enrollment period, as of November 30, the number of plan selections made through the exchange was 23% higher than at the same point last year. Average premiums also have increased between the plan years along with a shift towards enrollees utilizing advanced premium tax credits (APTC) and/or cost sharing reductions (CSR).

Currently, C4HCO is undergoing a program audit by the Colorado Office of the State Auditor as mandated by the legislature and an audit of the federal grant fund expenditures by the Department of Health and Human Services Office of Inspector General.

The organization is currently in the process of revising its strategic plan. One of the major goals for the process is to determine the necessary steps to achieving long-term sustainability for the organization. Management will work closely with staff, the Board and the Legislative Oversight Committee in the development of the plan with opportunities for public input.

Contacting Colorado Health Benefit's Financial Management

This Management's Discussion and Analysis, the accompanying financial statements, the notes to the financial statements, and the single audit section are designed to provide readers with a general overview of Colorado Health Benefit Exchange's finances and to reflect accountability and financial transparency relating to funds received and expenditures of those funds. If you have questions about this report or need additional financial information, please contact the organization's financial team at the corporate offices. Contact information may be found on the website at www.connectforhealthco.com.

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Colorado Health Benefit Exchange Statements of Net Position June 30, 2016 and 2015

| | 2016 | 2015 |
|--|---------------|--------------|
| Assets: | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 12,745,709 | 33,741,071 |
| Accounts receivable, net of allowance for doubtful accounts of \$123,966 in 2016 and \$33,201 in 2015 | 12,774,535 | 6,136,214 |
| Prepaid expenses | 2,706,305 | 2,888,962 |
| Total current assets | 28,226,549 | 42,766,247 |
| Noncurrent assets: | | |
| Security deposits | 36,535 | 18,719 |
| Long-term portion of prepaid expenses | 1,400,256 | 3,020,387 |
| Total noncurrent assets | 1,436,791 | 3,039,106 |
| Capital assets (note 2): | | |
| Web portal development | 36,228,577 | 32,687,048 |
| Software | 18,819,730 | 16,209,994 |
| Leasehold improvements | 1,943,642 | 1,943,642 |
| Office equipment | 1,117,696 | 1,083,698 |
| Furniture and fixtures | 833,776 | 833,776 |
| | 58,943,421 | 52,758,158 |
| Less accumulated depreciation and amortization | (28,088,422) | (15,517,072) |
| Capital assets, net | 30,854,999 | 37,241,086 |
| Total assets | \$ 60,518,339 | 83,046,439 |
| Liabilities: | | |
| Current liabilities: | | |
| Accounts payable | \$ 3,666,229 | 7,564,485 |
| Accrued liabilities | 265,593 | 566,092 |
| Payroll liabilities | 330,370 | 220,109 |
| Unearned revenue | - | 5,123,051 |
| Total current liabilities | 4,262,192 | 13,473,737 |
| Long-term liabilities: | | |
| Long-term portion of unearned revenue | 47,874 | 38,378 |
| Total liabilities | 4,310,066 | 13,512,115 |
| Net Position: | | |
| Net investment in capital assets | 30,854,999 | 37,241,086 |
| Restricted (note 1(g)) | 183,750 | - |
| Unrestricted | 25,169,524 | 32,293,238 |
| Total net position | 56,208,273 | 69,534,324 |
| Commitments and contingency (notes 4, 5 and 6) | | |
| Total liabilities and net position | \$ 60,518,339 | 83,046,439 |

See the accompanying notes to the financial statements.

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Colorado Health Benefit Exchange Statements of Revenues, Expenses, and Changes in Net Position Years Ended June 30, 2016 and 2015

| | <u>2016</u> | <u>2015</u> |
|--|----------------------|-------------------|
| Operating Revenues: | | |
| Federal grants | \$ 5,346,702 | 45,815,793 |
| Other grants and contributions | 3,063,800 | 3,032,245 |
| Program revenue (note 3) | 22,178,323 | 26,398,708 |
| Fees for service | 14,664,752 | 6,863,548 |
| Interest income | 22,950 | 45,799 |
| Other revenue | 109,772 | 20,161 |
| | <u>45,386,299</u> | <u>82,176,254</u> |
| Operating Expenses: | | |
| Customer service | 17,436,973 | 20,844,789 |
| Depreciation and amortization | 12,571,350 | 9,519,628 |
| Technology development | 12,355,107 | 13,689,543 |
| Salaries, payroll taxes, and benefits | 7,347,143 | 5,318,520 |
| Professional services | 3,709,953 | 4,790,577 |
| Assistance network | 2,755,762 | 7,795,220 |
| Marketing and outreach | 1,052,820 | 4,659,798 |
| Other | 620,762 | 498,317 |
| Occupancy | 496,641 | 446,612 |
| Supplies and equipment | 139,583 | 133,901 |
| Training | 135,491 | 335,185 |
| Bad debt | 90,765 | 33,201 |
| | <u>58,712,350</u> | <u>68,065,291</u> |
| Increase (decrease) in net position | (13,326,051) | 14,110,963 |
| Net position at beginning of year | <u>69,534,324</u> | <u>55,423,361</u> |
| Net position at end of year | <u>\$ 56,208,273</u> | <u>69,534,324</u> |

See the accompanying notes to the financial statements.

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Colorado Health Benefit Exchange Statements of Cash Flows Years Ended June 30, 2016 and 2015

| | <u>2016</u> | <u>2015</u> |
|---|------------------------|---------------------|
| Cash flows from operating activities: | | |
| Federal grants received | \$ 220,626 | 60,480,227 |
| Other grants and contributions received | 3,063,800 | 2,500,000 |
| Other operating revenue received | 30,259,232 | 29,408,190 |
| Cash paid for federal grants to subrecipients | – | (4,712,409) |
| Cash paid to vendors for materials and services | (41,116,875) | (56,882,179) |
| Cash paid to employees for wages, taxes and benefits | (7,236,882) | (5,282,590) |
| Net cash provided by (used in) operating activities | <u>(14,810,099)</u> | <u>25,511,239</u> |
| Cash flows used in capital and related financing activities: | | |
| Purchases of capital assets | <u>(6,185,263)</u> | <u>(12,951,637)</u> |
| Net cash used in capital and related financing activities | <u>(6,185,263)</u> | <u>(12,951,637)</u> |
| Net increase (decrease) in cash and cash equivalents | (20,995,362) | 12,559,602 |
| Cash and cash equivalents at beginning of year | <u>33,741,071</u> | <u>21,181,469</u> |
| Cash and cash equivalents at end of year | <u>\$ 12,745,709</u> | <u>33,741,071</u> |
| Reconciliation of increase in net position to net cash provided by (used in) operating activities: | | |
| Increase (decrease) in net position | \$ (13,326,051) | 14,110,963 |
| Adjustments to reconcile increase in net position to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 12,571,350 | 9,519,628 |
| Provision for doubtful accounts | 90,765 | 33,201 |
| Decrease (increase) in operating assets: | | |
| Accounts receivable | (6,729,086) | (3,923,611) |
| Federal grants receivable | – | 16,455,727 |
| Prepaid expenses | 1,802,788 | 1,047,435 |
| Security deposits | (17,816) | 1,000 |
| Decrease in operating liabilities: | | |
| Accounts payable and accrued liabilities | (4,088,494) | (9,413,151) |
| Unearned revenue | (5,113,555) | (2,319,953) |
| Net cash provided by (used in) operating activities | <u>\$ (14,810,099)</u> | <u>25,511,239</u> |

See the accompanying notes to the financial statements.

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Colorado Health Benefit Exchange Notes to Financial Statements June 30, 2016 and 2015

(1) Summary of Significant Accounting Policies

(a) Organization

In 2011, the Colorado General Assembly passed, and the Governor signed into law, Senate Bill 11-200, which authorized the creation of Colorado Health Benefit Exchange (the Exchange) for the purpose of establishing a state health insurance exchange in compliance with the Patient Protection and Affordable Care Act (ACA) of 2010. The Exchange was organized as an instrumentality of the State and further defined as a nonprofit corporation created to facilitate a health benefit exchange to increase access, affordability, and choice for individuals and small employers purchasing health insurance in Colorado.

Federal grant funding is being provided to finance the Exchange design, development, and implementation phases. This funding began in 2011 and ended June 30, 2016. The Exchange began conducting business in October 2013.

During the year ended June 30, 2013, the Exchange began doing business as Connect for Health Colorado.

(b) Basis of Accounting

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America for proprietary (enterprise) funds. The financial statements have been presented on the economic resources measurement focus and the accrual basis of accounting. Accordingly, revenues are recognized when earned and expenses are recognized when incurred. The Exchange has adopted the pronouncements of the Governmental Accounting Standards Board (GASB).

(c) Cash Equivalents

For purposes of the statements of cash flows, the Exchange considers all unrestricted highly liquid investments with original maturities of three months or less to be cash equivalents.

(d) Accounts Receivable

The change in net position is charged with an allowance for estimated uncollectible accounts based on an analysis of current accounts receivable collectability. Accounts deemed uncollectible are charged to the change in net position when that determination is made. At June 30, 2016 and 2015, the Exchange has recognized an allowance of \$123,966 and \$33,201, respectively.

(e) Capital Assets

The Exchange follows the practice of capitalizing, at cost, all expenditures for capital assets in excess of \$5,000 and groups of lower cost assets that exceed \$5,000, as well as donations of capital assets, with estimated fair values exceeding \$5,000, at the date of donation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets ranging from five to seven years.

Colorado Health Benefit Exchange

Notes to Financial Statements, Continued

(1) Summary of Significant Accounting Policies, Continued

(f) Federal Grant Revenue

Federal grant revenue is recognized as related expenses are incurred and work is performed. Any funding received in advance is recorded as unearned revenue. At June 30, 2016, there is no unearned revenue related to federal grant funds. At June 30, 2015, federal grant funds received in advance and recognized as unearned revenue total \$5,120,886.

(g) Net Position

Net position represents all assets, less liabilities. Net position is displayed in the statements of net position in the following categories:

Net investment in capital assets: Capital assets, net of accumulated depreciation.

Restricted: Net position where there are limitations on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments. At June 30, 2016, restricted net position totals \$183,750 and consists of grant funds received that are restricted for a specific purpose and have not yet been spent. At June 30, 2015, there is no restricted net position.

Unrestricted: All remaining net position that does not meet the definition of “net investment in capital assets” or “restricted”.

(h) Operating Revenue and Expenses

The Exchange distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses include all items related to establishing and running a health insurance marketplace. There were no non-operating items for the years ended June 30, 2016 and 2015.

(i) Concentrations of Credit Risk

Financial instruments which potentially subject the Exchange to concentrations of credit risk consist of cash and federal grants receivable. The Exchange’s bank accounts at year-end were entirely covered by federal depository insurance or by collateral held by the Exchange’s custodial banks under provisions of the Colorado Public Deposit Protection Act (PDPA). PDPA requires financial institutions to pledge collateral having a market value of at least 102% of the aggregate public deposits not incurred by federal depository insurance. Eligible collateral includes municipal bonds, U.S. government securities, mortgages, and deeds of trust.

The Exchange receives a significant portion of its revenue from federal grants and state-mandated funding under House Bill 13-1245 (see note 3). This revenue is contingent upon future approval of funding and appropriation by the government. If a significant reduction in the level of this support occurs, it would have a significant effect on the Exchange’s programs and activities.

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Colorado Health Benefit Exchange

Notes to Financial Statements, Continued

(1) Summary of Significant Accounting Policies, Continued

(j) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure on contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(k) Risk Management

The Exchange is subject to the risk of loss from various events, including, but not limited to, natural disasters and destruction of assets. The Exchange is currently covered by a commercial insurance program that contains multiple individual policies to mitigate risk exposure. Settled claims from these risks have not exceeded the insurance coverage in any of the past fiscal years.

(l) Subsequent Events

Management is required to evaluate, through the date the financial statements are issued or available to be issued, events or transactions that may require recognition or disclosure in the financial statements, and to disclose the date through which subsequent events were evaluated. The Exchange's financial statements were available to be issued on January 9, 2017, and this is the date through which subsequent events were evaluated.

(2) Capital Assets

Following are the changes in capital assets:

| | July 1, 2014 | Additions | Retirements | June 30, 2015 |
|---|----------------------|--------------------|-------------|---------------------|
| Web portal development | \$ 24,444,591 | 8,242,457 | — | 32,687,048 |
| Software | 11,611,102 | 4,598,892 | — | 16,209,994 |
| Leasehold improvements | 1,912,952 | 30,690 | — | 1,943,642 |
| Office equipment | 1,063,252 | 20,446 | — | 1,083,698 |
| Furniture and fixtures | <u>774,624</u> | <u>59,152</u> | <u>—</u> | <u>833,776</u> |
| | 39,806,521 | 12,951,637 | — | 52,758,158 |
| Less accumulated depreciation and amortization | <u>(5,997,444)</u> | <u>(9,519,628)</u> | <u>—</u> | <u>(15,517,072)</u> |
| Capital assets, net | \$ <u>33,809,077</u> | <u>3,432,009</u> | <u>—</u> | <u>37,241,086</u> |

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Colorado Health Benefit Exchange

Notes to Financial Statements, Continued

(2) Capital Assets, Continued

| | July 1, <u>2015</u> | <u>Additions</u> | <u>Retirements</u> | June 30, <u>2016</u> |
|---|------------------------|---------------------|--------------------|-------------------------|
| Web portal development | \$ 32,687,048 | 3,541,529 | — | 36,228,577 |
| Software | 16,209,994 | 2,609,736 | — | 18,819,730 |
| Leasehold improvements | 1,943,642 | — | — | 1,943,642 |
| Office equipment | 1,083,698 | 33,998 | — | 1,117,696 |
| Furniture and fixtures | <u>833,776</u> | <u>—</u> | <u>—</u> | <u>833,776</u> |
| | 52,758,158 | 6,185,263 | — | 58,943,421 |
| Less accumulated depreciation and amortization | <u>(15,517,072)</u> | <u>(12,571,350)</u> | <u>—</u> | <u>(28,088,422)</u> |
| Capital assets, net | <u>\$ 37,241,086</u> | <u>(6,386,087)</u> | <u>—</u> | <u>30,854,999</u> |

(3) House Bill 13-1245

On May 6, 2013, the State of Colorado General Assembly passed House Bill 13-245, which outlines funding mechanisms that will help to support the Exchange in the short and long terms. Specifically, the House Bill allows for three components of the Exchange's future revenue approach. First, it allows for a fee to be placed on insurance carriers, which is not allowed to exceed \$1.80 per number of lives insured per month. Effective January 1, 2015, the Exchange assessed a fee of \$1.25 per number of lives insured per month. The Exchange then raised this fee to \$1.80 per number of lives insured per month, effective January 1, 2016. The Exchange has the option to exercise this fee assessment through December 2016. Second, the House Bill allows for a portion of reserves collected from the closing of CoverColorado to be transferred to the Exchange to fund operations. Lastly, any deductible donations made by insurance carriers, which have been directed to CoverColorado in the past, will now be pledged to the Exchange. Revenues recognized under House Bill 13-1245 totaled \$22,178,323 and \$26,398,708 for the years ended June 30, 2016 and 2015, respectively, and are included in program revenue in the Statements of Revenues, Expenses, and Changes in Net Position.

(4) Leases

The Exchange has a non-cancelable operating lease for office space in Denver, Colorado, which requires monthly payments totaling \$42,153, and is scheduled to expire in March 2018. Furthermore, the Exchange has a cancelable operating lease for office space in Colorado Springs, Colorado, which is being used for its call center. This lease is scheduled to expire in August 2020, unless the cancellation option is exercised, which requires 90 days notice. The Exchange is also obligated under a non-cancelable copier lease which requires monthly payments of \$1,882 and expires June 2018. Future minimum lease payments under non-cancelable operating leases are as follows for the years ended June 30:

| | |
|------|-------------------|
| 2017 | \$ 528,426 |
| 2018 | <u>401,965</u> |
| | <u>\$ 930,391</u> |

Colorado Health Benefit Exchange

Notes to Financial Statements, Continued

(4) Leases, Continued

Lease expense in the accompanying financial statements is being recognized on the straight-line method, evenly over the term of each lease. Total rent expense for office space for the years ended June 30, 2016 and 2015 was \$646,728 and \$591,165, respectively. Total rent expense for the copier lease for the years ended June 30, 2016 and 2015 was \$28,902 and \$27,169, respectively.

(5) Retirement Plan

The Exchange established a retirement plan under section 403(b) of the Internal Revenue Service Code that is available to its employees. The Exchange contributes 5% of employee salaries for eligible employees. In addition, the Exchange matches 100% of the employee's elective deferral amount that does not exceed 5% of the total employee's compensation. Employees are 100% vested in their account balance after one year of service. Total employer contributions under this plan for the Exchange were \$507,830 for the year ended June 30, 2016 and \$353,963 for the year ended June 30, 2015.

(6) Contingency

The Exchange is a recipient of federal and state awards which are subject to audit to determine compliance with applicable regulations. On December 27, 2016, the Exchange received an audit report from the Department of Health and Human Services Office of the Inspector General recommending the refund of \$9,678,635 in questioned federal expenditures from 2012 to 2014. A significant portion of these expenditures had been previously identified as unallowable by the Exchange and, as a result, reimbursement requests made under the federal grant in previous periods were reduced for the unallowable expenditures identified. Connect for Health Colorado is in the process of responding to the findings with federal officials and believes there is sufficient evidence to support the allowance of the questioned costs under the federal program of the remaining questioned costs that were identified. While the maximum amount of the possible loss can be reasonably estimated at this time, management believes that it is reasonably possible (but not probable) that a loss has occurred. Therefore, a liability has not been recognized for these questioned costs as of June 30, 2016.

**Independent Auditor’s Report on Internal Control over Financial Reporting and on
Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance with Government Auditing Standards**

**Board of Directors
Colorado Health Benefit Exchange:**

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Colorado Health Benefit Exchange (the Exchange), which comprise the statement of net position as of June 30, 2016, and the related statements of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 19, 2016.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Exchange’s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Exchange’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Exchange’s internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Exchange’s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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Board of Directors Colorado Health Benefit Exchange

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

January 9, 2017

Independent Auditor's Report on Compliance for Each Major Program and on Internal Control over Compliance Required by the Uniform Guidance

Board of Directors Colorado Health Benefit Exchange:

Report on Compliance for Each Major Federal Program

We have audited Colorado Health Benefit Exchange's (the Exchange's) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Exchange's major federal programs for the year ended June 30, 2016. The Exchange's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Exchange's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Exchange's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Exchange's compliance.

Opinion on Each Major Federal Program

In our opinion, the Exchange complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with the Uniform Guidance and which is described in the accompanying schedule of findings and questioned costs as item 2016-001. Our opinion on each major federal program is not modified with respect to these matters.

The Exchange's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Exchange's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Board of Directors Colorado Health Benefit Exchange

Report on Internal Control over Compliance

Management of the Exchange is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Exchange's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Exchange's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified a certain deficiency in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item 2016-001, that we consider to be a significant deficiency.

The Exchange's response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The Exchange's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

January 9, 2017

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Colorado Health Benefit Exchange Schedule of Expenditures of Federal Awards Year Ended June 30, 2016

| <u>Federal grantor/pass-through grantor/program title</u> | <u>Grant Number</u> | <u>Federal award year</u> | <u>Federal CFDA number</u> | <u>Federal expend- itures</u> |
|--|---------------------|-------------------------------|------------------------------------|---------------------------------------|
| <i>U.S. Department of Health and Human Services:</i> | | | | |
| State Planning and Establishment | | | | |
| Grants for the Affordable Care | | | | |
| Act (ACA)'s Exchanges | HBEIE130169-01 | 7/9/13-6/30/16 | 93.525 | \$ <u>5,346,702</u> |
| <i>Total U.S. Department of Health and Human Services</i> | | | | <u>5,346,702</u> |
| Total Expenditures of Federal Awards | | | | \$ <u><u>5,346,702</u></u> |

Notes to the Schedule of Expenditures of Federal Awards:

Note (1) Basis of Presentation:

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal award activity of Colorado Health Benefit Exchange (the Exchange) under programs of the federal government for the year ended June 30, 2016. The information in this Schedule is presented in accordance with the requirements of Title 2 *U.S. Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the Exchange, it is not intended to and does not present the net position, changes in net position, or cash flows of the Exchange.

Note (2) Summary of Significant Accounting Policies:

Expenditures reported in the Schedule are reported on the accrual basis of accounting. All grant agreements were entered into prior to December 26, 2014 and, therefore, such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, and OMB Circular A-122, *Cost Principles for Non-Profit Organizations*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Note (3) Indirect Cost Rate:

Federal programs for the Exchange are limited to a grant received prior to December 26, 2014, which is not subject to Uniform Guidance. The Exchange does not have a negotiated indirect cost rate nor have they received any de minimis indirect cost rate under this agreement.

Note (4) Subrecipient Awards:

There were no awards passed through by the Exchange to subrecipients.

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Colorado Health Benefit Exchange
Schedule of Findings and Questioned Costs
Year Ended June 30, 2016

A. Summary of Auditor's Results

1. The auditor's report expresses an unmodified opinion on whether the financial statements of Colorado Health Benefit Exchange (the Exchange) were prepared in accordance with GAAP.
2. No significant deficiencies relating to the audit of the financial statements are reported in the *Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards*.
3. No instances of noncompliance material to the financial statements of the Exchange were disclosed during the audit.
4. One significant deficiency in internal control over major federal award programs disclosed during the audit is reported in the *Independent Auditor's Report on Compliance for Each Major Program and on Internal Control over Compliance Required by the Uniform Guidance*. No material weaknesses are reported.
5. The auditor's report on compliance for the major federal award program for the Exchange expresses an unmodified opinion on all major federal programs.
6. Audit findings that are required to be reported in accordance with 2 CFR section 200.516(a) are reported in this Schedule.
7. The major program tested was State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges (CFDA No. 93.525).
8. The threshold used for distinguishing between Type A and B programs was \$750,000.
9. The Exchange did not qualify as a low-risk auditee.

B. Findings—Financial Statements Audit

None.

C. Findings and Questioned Costs—Major Federal Award Programs Audit

2016-001 U.S. Department of Health and Human Services
CFDA No. 93.525 State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges
Procurement, Suspension and Debarment - Significant Deficiency

Criteria: OMB Circular A-110 requires that records are maintained that sufficiently detail the procurement process. For instance, these standards require that records are maintained to sufficiently detail the history of procurement. The records should include, but are not limited to the rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price. Additionally, all procurement transactions must be conducted in a manner providing full and open competition consistent with federal standards and requirements. Standards also require that some form of cost or price analysis be made and documented in the procurement files in connection with every procurement action.

Procurement by noncompetitive proposals is procurement through solicitation of a proposal from only one source and may be used only when certain criteria apply. This includes circumstances showing that the item is only available from a single source.

Condition: During fiscal 2016, expenditures totaling \$3,095,896 were applied to the federal grant, under three separate contracts, related to improvements made to the Shared Eligibility System (SES). The Exchange believed that procurement was permitted by

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Colorado Health Benefit Exchange
Schedule of Findings and Questioned Costs, Continued
Year Ended June 30, 2016

noncompetitive proposals for the three contracts as the services were only available from the sources used. However, the Exchange was unable to provide supporting records that detailed the history of procurement and basis for selection of the vendors, including documentation supporting that the contractors met the criteria to be chosen through noncompetitive proposals.

Also, as part of the procurement process, the Exchange requires Board approval for contracts over \$150,000. Board approval was noted for the entire SES project, with a maximum placed on project expenses by the Board. However, board approval was not obtained for each individual contract.

Questioned Costs: During fiscal 2016, federal expenditures charged to the federal grant under the contracts totaled \$3,095,896.

Cause: The Exchange failed to properly document the procurement process for the contracts and also failed to obtain proper Board approval for the contracts.

Effect: The Exchange lacks proper records that detail the procurement process followed for the contracts, as required by OMB Circular A-110.

Recommendation: The Exchange should implement proper procedures that allow for thorough documentation of the procurement process, in accordance with OMB Circular A-110. Furthermore, the Exchange should adhere to its policy, requiring approval by the Board for any contract in excess of \$150,000.

Views of Responsible Officials and Planned Corrective Actions: In response to a similar finding in the prior year audit, Connect for Health successfully implemented new procurement procedures during fiscal year 2016 to improve the documentation of the contract/procurement process. These new procedures were implemented subsequent to the procurement of the contracts in this finding.

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Colorado Health Benefit Exchange
Summary Schedule of Prior Audit Findings
Year Ended June 30, 2016

2015-001 Controls over Financial Reporting (Material Weakness)

Condition: Our audit resulted in four significant audit adjustments, which indicated an opportunity for improved internal control over financial statement reporting. The Exchange failed to apply the proper accounting treatment to items, in accordance with generally accepted accounting principles, and also failed to recognize items in the proper accounting period. Furthermore, the Exchange did not perform proper reconciliations of activity related to premiums collected on behalf of carriers and the related fees collected by the Exchange.

Recommendation: Consideration should be given to new activity and accounting transactions, as to the proper accounting treatment that should be applied, in accordance with generally accepted accounting principles. Final, signed contracts and other supporting documentation should be obtained in a timely manner, prior to incurring cost, in order to determine the proper accounting treatment of costs. Also, accounting should review costs to determine that they are recognized in the appropriate accounting period. Timely reconciliations should also be performed of activity related to premiums collected on behalf of carriers and the related fees collected by the Exchange. Finally, the financial statements should be reviewed thoroughly by management to determine proper inclusion and treatment of all activity.

Current Status: The recommendation was implemented. No significant audit adjustments were required as part of the current year audit.

2015-002 U.S. Department of Health and Human Services
CFDA No. 93.525 State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges
Activities Allowed and Allowable Costs, Cash Management, and Reporting – Material Weakness

Condition: Subsequent to claims made throughout the year and subsequent to year-end, the Exchange made numerous corrections to reallocate unallowable costs under the federal grant to other funding. Most of these unallowable costs consisted of operating costs being charged to the grant after January 1, 2015, which was unallowable under the grant. Also, adjustments were made for costs that were determined to be unallowable under audits conducted on the Exchange. Due to inadequate controls in place, the unallowable costs were not identified in a timely manner, allowing for federal funds to be drawn and disbursed for payment. As a result of the untimely corrections, a liability totaling \$6,613,885 had been recognized as of June 30, 2015 for amounts due under the federal grant. Federal grant recipients are required to implement procedures to minimize the time elapsing between the transfer and disbursement of federal funds.

Additionally, under the federal grant, the Exchange is required to file quarterly Federal Financial Reports (FFR) on the Standard Form 425, as well as monthly budget to actual reports with the federal agency. The Exchange also relies internally on the budget to actual report to monitor its spending on the federal grant. Both of these reports require cumulative financial information to be presented. However, as a result of the untimely corrections made, the financial amounts reported on the required reports were inaccurate and not corrected by the Exchange.

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Colorado Health Benefit Exchange
Schedule of Findings and Questioned Costs, Continued
Year Ended June 30, 2016

Recommendation: Proper controls should be implemented to allow for identification of unallowable costs in a timely manner. Employees with procurement responsibility should be adequately trained and able to identify unallowable costs under the federal program. Furthermore, the Exchange should discuss with the federal agency and document whether funds overdrawn on the grant should be returned or whether the Exchange can continue to spend down the funds. The Exchange should also consider filing amended reports.

Current Status: The recommendation was fully implemented. During 2016, the Exchange continued to apply federal expenditures to the liability of amounts due to the federal government. No cash draws were made on the grant until the liability was fully reduced. Also, no unallowable costs were identified as part of the audit and there were no findings related to reporting.

- 2015-003 U.S. Department of Health and Human Services
CFDA No. 93.525 State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges
Activities Allowed and Allowable Costs – Significant Deficiency

Condition: Under OMB Circular A-110, the “cost-plus-a-percentage-of-cost” method of contracting is not allowed. The “cost-plus-a-percentage-of-cost” is a method of contracting or a type of contract under which the contractor is not only reimbursed his performance costs but is also paid a stated percentage of the costs. The Exchange entered into two contracts with one of its vendors for media placement services which required reimbursement for media buys, as well as fees to be paid to the vendor at 8% of the media placement buys. This was a repeat of prior year finding 2014-006.

Recommendation: Employees with procurement responsibility should be adequately trained and able to identify unallowable costs under the federal program.

Current Status: The recommendation as fully implemented. There were no similar findings noted in the current year audit.

- 2015-004 U.S. Department of Health and Human Services
CFDA No. 93.525 State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges
Subrecipient Monitoring – Significant Deficiency

Condition: For one of the three subrecipient audits reviewed as part of the audit, the subrecipient did not list the federal award provided by the Exchange on its Schedule of Expenditures of Federal Awards, which expended \$319,903 in federal expenditures during the fiscal year under review. Therefore, the subrecipient failed to include these expenditures in their OMB Circular A-133 audit and, as a result, did not accurately meet the audit requirements under OMB Circular A-133. The Exchange was unable to provide documentation showing that this error was followed up on and subsequently corrected by the subrecipient. Also, during fiscal 2015, the Exchange used non-federal sources of funding to reimburse some of the expenses under the subawards. However, the Exchange did not have a policy in place to identify to the subrecipients the portion of funding attributable to federal sources of funding vs. non-federal sources. This results in inaccurate reporting of federal expenditures for the subrecipient audits and could result in deficient audits being performed under OMB Circular A-133. Also, this leads to inaccurate reporting under the Federal Funding Accountability and Transparency Act,

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Colorado Health Benefit Exchange
Schedule of Findings and Questioned Costs, Continued
Year Ended June 30, 2016

through which the Exchange must report total federal subaward amounts that are awarded to subrecipients.

Recommendation: The Exchange should establish internal control procedures that ensure subrecipient audits are properly reviewed to ensure compliance with OMB Circular A-133. Also, the Exchange should implement procedures that allow for proper identification of federal award amounts to subrecipients and should consider specifically identifying these amounts within subaward agreements.

Current Status: This compliance area did not apply to the current year audit as no subrecipient grants were given under the federal grant for 2016.

- 2015-005 U.S. Department of Health and Human Services
CFDA No. 93.525 State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges
Reporting – Significant Deficiency

Condition: In follow-up to prior year finding 2014-004, the required FFATA reporting was reviewed for subawards issued in July 2013. The report was originally submitted in April 2015 and subsequently corrected in February and March 2016. Review of the report showed that incorrect federal subaward amounts were reported for the subrecipients. The Exchange had reported cumulative federal expenditures to date under the subawards. However, the total approved federal award amount under the subaward was required to be reported. Additionally, as a result of finding 2015-004 above, it was unclear what amounts should be reported as the approved federal funding amounts under the awards had not been specifically identified.

Recommendation: The Exchange should revise the FFATA report previously issued to reflect accurate amounts. Additionally, the Exchange should implement control procedures to ensure that reporting requirements are met timely and accurately in the future.

Current Status: Reporting under FFATA was not required for 2016. However, a revised report for the July 2013 subawards was properly filed by the Exchange, reflecting subaward amounts.

- 2015-006 U.S. Department of Health and Human Services
CFDA No. 93.525 State Planning and Establishment Grants for the Affordable Care Act (ACA)'s Exchanges
Procurement, Suspension and Debarment - Significant Deficiency

Condition: OMB Circular A-110 requires that records are maintained that sufficiently detail the procurement process. For instance, these standards require that records are maintained to sufficiently detail the history of procurement. The records should include, but are not limited to the rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price. Additionally, all procurement transactions must be conducted in a manner providing full and open competition consistent with federal standards and requirements. Standards also require that some form of cost or price analysis be made and documented in the procurement files in connection with every procurement action.

DRAFT
Colorado Health Benefit Exchange
Schedule of Findings and Questioned Costs, Continued
Year Ended June 30, 2016

During fiscal 2015, the Exchange entered into two large contracts with a vendor, totaling \$6,048,000, to provide media placement services. As part of the procurement process, the Exchange provided a memo to the Board briefly describing the procurement process and specifying that three separate vendors were reviewed in the process. However, the Exchange was unable to provide supporting records that detailed the history of procurement, including descriptive information of the three vendors reviewed, basis of selection or rejection for the vendors, cost analysis, and evidence that an open proposal process was followed.

Also, as part of the procurement process, the Exchange requires Board approval for contracts over \$150,000. Board approval was noted for one of the contracts, totaling \$1,998,000. However, the Exchange was unable to provide evidence of Board approval for the other contract, totaling \$4,050,000.

Recommendation: The Exchange should implement proper procedures that allow for thorough documentation of the procurement process, in accordance with OMB Circular A-110. Furthermore, the Exchange should adhere to its policy, requiring approval by the Board for any contract in excess of \$150,000.

Current Status: Not implemented. See current year finding 2016-001.

DRAFT

12/19/2016

To Management of
Colorado Health Benefit Exchange:

In planning and performing our audit of the financial statements of Colorado Health Benefit Exchange (the Exchange) as of and for the year ended June 30, 2016, in accordance with auditing standards generally accepted in the United States of America, we considered the Exchange's internal control over financial reporting (internal control) as a basis for designing our auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Exchange's internal control. Accordingly, we do not express an opinion on the effectiveness of the Exchange's internal control.

During our audit of the Exchange, we became aware of several matters that are not internal control deficiencies required to be reported under generally accepted auditing standards, but warrant the attention of management. The attachment that accompanies this letter summarizes our comments and suggestions regarding those matters.

This communication is intended solely for the information and use of management, the board of directors, and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

January 9, 2017

DRAFT
Colorado Health Benefit Exchange
Operational Matters Letter
Year Ended June 30, 2016

Current Year Comment

- 1) During 2016, a corporate credit card was issued to the Executive Director. As part of the audit, one month of expenses charged to the Executive Director's credit card were tested for proper support, business purpose, and proper approval by a board member. For five of the eight purchases charged to the credit card, an original receipt was not obtained in support of the purchase. Also, the business purpose was not described for the purchases made. Lastly, board approval was noted for the charges, but it was obtained seven months after the purchases were made. We recommend that proper documentation supporting all charges should be attached to each credit card statement. Additionally, business purpose for each expense should be briefly described. Also, board review and approval can be performed after the fact rather than prior to payment, but should be done on a timely basis.

Prior Year Comments

- 1) Any cash receipts received through the mail (i.e. checks) are required to be recorded by the Office Manager in a cash receipts log. The cash receipts log is then later reconciled to the final deposit within the Exchange's bank account by the Office Manager. This process allows for proper segregation of duties and strengthens internal controls over cash receipts. However, during our testing, we noted that not all cash receipts are being recorded within the cash receipts log, as required. Also, the cash receipts log is not being reconciled to the final deposit within the Exchange's bank account. We recommend that the Exchange adhere to its policy, requiring all cash receipts received by mail to be recorded in the cash receipts log and later reconciled to the final deposit.

Status: Implemented. A cash receipts log is now being properly used to record cash receipts received by mail and is later being reconciled to the final deposit.

- 2) The Exchange only operates one program related to the establishment and operating of a state health insurance exchange. As a result, all employees spend their time on the one program and all salaries are reimbursable under the federal grant. Therefore, employees of the Exchange have not documented the allocation of their time by program, as normally required by federal cost principles. However, OMB Circular A-87 requires that, where employees are expected to work solely on a single Federal award, charges for their salaries should be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications should be prepared at least semi-annually and should be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee. The Exchange should require their employees to complete these certifications, in accordance with OMB Circular A-87. Also, where possible, this policy should be retroactively implemented.

Additionally, beginning January 1, 2015, operational costs are no longer allowed to be charged to the federal grant. The Exchange did not allocate any salaries to the federal grant for the period January 1, 2015 through June 30, 2015. However, if the Exchange does elect in the future to charge salaries and related expenses to the federal grant, employees should then properly document and allocate their time between operational vs. non-operational activities, in accordance with requirements under federal costs principles.

Status: Not applicable. This compliance area did not apply to the current year audit as no salaries were charged to the federal grant during fiscal 2016.

DRAFT
Colorado Health Benefit Exchange
Operational Matters Letter
Year Ended June 30, 2016

- 3) As a result of our audit, several unallowable costs were identified as being charged to the federal grant, but not required to be reported in the “Schedule of Findings and Questioned Costs” as they did not meet the \$25,000 reporting threshold. First, retention bonuses, totaling \$23,500 were paid to select employees during the year and charged to the federal grant. Incentive compensation is allowable to the extent that the overall compensation is determined to be reasonable and such costs are paid or accrued pursuant to an agreement entered into in good faith between the entity and the employees before the services were rendered, or pursuant to an established plan followed by the entity so consistently as to imply, in effect, an agreement to make such payment. The retention bonuses paid were not for specific services rendered, were paid to only select employees, and not paid through an established policy of the Exchange. Also, an expense of \$2,700 was charged to the grant which included services regarding promotional giveaways, a cost specifically identified as unallowable under the federal grant. Finally, an expense of \$2,700 was charged to the grant for the monthly rental of a vehicle. However, the business purpose of the rental was not properly documented with the payment. Internal controls should be implemented as to allow for proper identification of unallowable costs in a timely manner.

Status: Implemented. No allowable costs were identified as part of the current year audit.

- 4) In order to monitor subrecipient spending under subawards, the Exchange completes rollforwards of subrecipient grant amounts that itemize the expenses reimbursed and compares the amounts to approved budgets. However, during fiscal 2015, these rollforwards were not effectively completed and utilized by the Exchange. Rather, only the fiscal 2015 amounts were compared to budgeted amounts and the itemized rollforwards did not properly include 2014 amounts. Because the grant periods cover both fiscal years, it is important that both years of expenses are included in the itemized rollforwards, in order to accurately compare budgeted amounts to actual reimbursements. This control is important to ensure that amounts reimbursed to subrecipients under the federal grant fall within approved budget amounts and are allowable. The Exchange should complete itemized rollforwards of each subrecipient grant, comparing actual reimbursements to approved budgeted amounts to ensure costs are allowable and agree to subaward agreements.

Status: Implemented. This compliance area did not apply to the federal grant for the current year audit as no subrecipient grants were made under the federal grant during fiscal 2016. However, grant rollforwards were reviewed in our testing of this expense and it was noted that the rollforwards are now itemized, comparing actual reimbursements to approved budgeted amounts.

- 5) Although the auditor may assist in preparing the Schedule of Expenditure of Federal Awards, the auditee is responsible for preparation of the schedule. The auditor then determines whether the Schedule of Expenditures of Federal Awards is presented fairly in all material respects in relation to the financial statements as a whole and issues a report on the schedule. A Schedule of Expenditure of Federal Awards was not entirely prepared by the Exchange prior to the audit. Rather, some of the schedule was compiled by us, using information provided as part of the audit. We recommended that personnel be properly trained to prepare the schedule and that, for future audits, the schedule be prepared by personnel prior to the audit.

Status: Not fully implemented. A Schedule of Expenditures of Federal Awards was prepared by the Exchange. However, the schedule initially reflected an incorrect amount for fiscal 2016 federal expenditures and had to be revised as part of the audit.

**Colorado Health Benefit Exchange
Communication with Those Charged with Governance
Regarding the June 30, 2016 Audit**

| AREA | COMMENT |
|---|--|
| Our Responsibility Under U.S. Generally Accepted Auditing Standards (GAAS) | Audit performed in accordance with GAAS. The objective of an audit is reasonable, but not absolute, assurance about whether the financials are free of material misstatement. Our audit does not relieve you or management of your responsibilities. |
| Other Information in Documents Containing Audited Financials | The financial statements include Single Audit required information for the year ended June 30, 2016. The financial statements include GASB 34-required Management Discussion and Analysis for the year ended June 30, 2016. |
| Planned Scope and Timing of Audit | The audit was performed according to the planned scope and timing previously communicated to you in our engagement letter dated August 23, 2016. |
| Significant Audit Findings | <ol style="list-style-type: none"> 1. Management has the responsibility for selection and use of appropriate accounting policies. The significant policies used (such as the basis of accounting, type of entity and the definition of operating revenue) are listed in Note 1 to the financial statements. 2. No new accounting policies were adopted during the year and the application of existing policies was not changed during the year. 3. We noted no transactions were entered into in 2016 with an absence of authoritative accounting guidance or consensus. 4. There were no significant transactions recognized in a different period than when the transaction occurred, other than uncorrected misstatement noted below. 5. Sensitive accounting estimates include the following: the collectibility of receivables, the receivable for carrier fees, the amortization period of deferred costs, and the depreciable lives of capitalized assets. 6. Financial statement disclosures are neutral, consistent and clear. |
| Difficulties Encountered in Performing the Audit | We encountered no significant difficulties in dealing with management in performing and completing our audit. |
| Corrected and Uncorrected Misstatements | Management has corrected all known and likely misstatements. No audit adjustments were made as part of the audit. An adjustment was not made, totaling \$149,850, to reverse expenses that had incurred in fiscal 2015, but were recorded in fiscal 2016, due to immateriality. |
| Disagreements with Management | No disagreements arose with management during the course of our audit on financial accounting, reporting or auditing matters. |

**Colorado Health Benefit Exchange
Communication with Those Charged with Governance, Continued
Regarding the June 30, 2016 Audit**

| AREA | COMMENT |
|--|--|
| Management Representations | We requested certain representations from management that are included in their representation letter dated January 9, 2017. |
| Management Consultations with Other Independent Accountants | We are not aware of any consultations by management with other accountants about accounting and auditing matters. |
| Other Audit Findings or Issues | There were no discussions of the application of certain accounting principles prior to our retention as auditor. |

This communication is intended solely for the use of the board of directors and management of the Exchange and is not intended to be, and should not be, used by anyone other than these specified parties.

January 9, 2017