



COMMONWEALTH HEALTH INSURANCE CONNECTOR AUTHORITY
(A Component Unit of the Commonwealth of Massachusetts)

Financial Statements and Required Supplementary Information

June 30, 2018

(With Independent Auditors' Report Thereon)



KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

Independent Auditors' Report

The Board of Directors
Commonwealth Health Insurance Connector Authority:

Report on the Financial Statements

We have audited the accompanying financial statements of the Commonwealth Health Insurance Connector Authority (the Health Connector), a component unit of the Commonwealth of Massachusetts, which comprise the Statement of Net Position, the Statements of Revenues, Expenses, and Changes in Net Position and Cash Flows as of and for the year ended June 30, 2018 and the related notes to the financial statements, which collectively comprise the Health Connector's basic financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles (GAAP); 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 auditors' 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 the Commonwealth Health Insurance Connector Authority as of June 30, 2018, and the changes in its financial position and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.



Emphasis of Matter

As discussed in note 1 to the financial statements, effective July 1, 2017, the Health Connector adopted Governmental Accounting Standards (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the Management's Discussion and Analysis on pages 3–7 and the Schedule of Proportionate Share of Net Pension Liability on page 23, and the Schedule of Changes in Total OPEB Liability and Related Ratios on page 24, be presented to supplement the basic financial statements. Such information, although not a 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 Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 7, 2018, on our consideration of the Health Connector'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 Health Connector's internal control over financial reporting and compliance.

KPMG LLP

Boston, Massachusetts
November 7, 2018

COMMONWEALTH HEALTH INSURANCE CONNECTOR AUTHORITY
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Management's Discussion and Analysis – Unaudited

June 30, 2018

Introduction

The following discussion of the financial performance and activity of the Commonwealth Health Insurance Connector Authority (the Health Connector) is intended to provide an overview and analysis of the basic financial statements for the fiscal year ended June 30, 2018. The management of the Health Connector has prepared this discussion and it should be read in conjunction with the financial statements and the notes thereto, which follow this section.

Background of the Health Connector

The Health Connector is a body politic and a corporate and public instrumentality of the Commonwealth of Massachusetts (the Commonwealth). The Health Connector is established pursuant to Chapter 176Q of the Massachusetts General Laws (MGLs), as added by Section 101 of Chapter 58 of the Acts of 2006, and is an independent public entity not subject to the supervision and control of any other office, department, commission, board, bureau, agency or political subdivision of the Commonwealth.

The Health Connector is governed by an eleven member public private Board, comprised of four ex-officio members – the Secretary of the Executive Office of Health and Human Services (EOHHS), who serves as chair of the Board; the Secretary of Administration and Finance; the Executive Director of the Group Insurance Commission (GIC); and the Commissioner of Insurance, as well as seven members of the public, four appointed by the Governor and three appointed by the Attorney General. Public sector members encompass a range of interests and expertise, including organized labor, employee health benefits, consumers, small business, actuarial science, health economics and health insurance brokerage.

The Health Connector's primary responsibility is to facilitate the availability, choice and adoption of private health insurance plans to eligible individuals and groups. Since January 1, 2014, the Health Connector has operated as a State-Based Marketplace (SBM) that meets the requirements of the Affordable Care Act (ACA). The Health Connector currently offers the following programs:

- Qualified Health Plans (QHPs) and Qualified Dental Plans (QDPs) for eligible individuals. Individuals with income up to 400% FPL may be eligible for federal Advanced Premium Tax Credits (APTC).
- ConnectorCare is a subsidized health insurance program offering QHPs to individuals at 300% or less of the FPL. In addition to federal tax credits, ConnectorCare members also receive state subsidies to further offset premium and point-of-service costs.
- Small Business Health Options Program (SHOP) offers QHPs and QDPs to small businesses. Small businesses may be eligible for ACA small business tax credits up to 50% of the cost of health insurance for businesses with fewer than 25 full time equivalent employees, who earn on average \$50,000 a year or less in 2018.
- The Navigator program is required by the ACA and provides grants to community organizations that assist consumers (individuals, families and small businesses), using culturally and linguistically appropriate methods, to learn about their health care coverage options; access any applicable federal tax credits and other state subsidies; and enroll in a health plan.

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- The Massachusetts-state-based risk adjustment program, the only state-specific program in the nation (federal certification received from CMS in March 2013). This program is administered by Massachusetts through Plan Year 2016 and as of Plan Year 2017 will be administered by the federal government.
- The Wellness Track program, established by Chapter 288 of the Acts of 2010, which allows eligible employers to earn up to a 15% rebate on the premium contribution for promoting a healthy workforce.

In addition, the Health Connector continues to be responsible for, among other things, policy development relative to the Affordability Schedule and Minimum Credible Coverage rules; administration of appeals filed on behalf of individuals in accordance with ConnectorCare program regulations and the Commonwealth's individual mandate; and public education and outreach activities.

Health Connector Operations

As of June 30, 2018, the Health Connector employed approximately 66 full-time equivalent personnel in business administration and program functions (i.e., finance, legal, operations, policy, outreach, plan management and information technology (IT)), as well as support functions, including an appeals unit to manage the appeals process for the individual mandate and ConnectorCare eligibility determinations. Additionally, the Health Connector subcontracts a significant amount of back office operations to public entities and private vendors, primarily IT development and maintenance and customer service and business operations.

The Health Connector has played a critical role in implementing the ACA in Massachusetts. Financing for ACA implementation efforts came in part from seven grants from the United States Department of Health and Human Services (HHS), including the Exchange Planning Grant and the Exchange Establishment grants totaling \$189.3 million. These funds primarily support one-time, ACA transition and implementation activities, which for FY2018 consisted of remaining implementation costs for SHOP.

Current Year Activities

In FY2018, the Health Connector continued to operate ACA-required programs that launched on January 1, 2014, including the offering of QHPs and QDPs to individuals and small businesses, the Navigator program and the Massachusetts-specific risk adjustment program. Many key accomplishments were achieved during FY2018, most notably a successful 2018 Open Enrollment that provided a stable customer experience for both new and renewing members. As of June 2018, there were over 252,190 individuals enrolled in QHPs and 5,654 small group QHPs. In addition, 80,018 of our QHP members were also enrolled in QDPs or were members with a dental only policy.

During FY2018, the Health Connector, along with the District of Columbia Health Benefit Exchange (DCHBX), completed an initial launch of the new Health Connector for Business (HCB) solution on August 15, 2017. Available to employers with fewer than 50 employees, HCB allows employers and employees to compare private health insurance options and management of benefits. The program is flexible in that it allows employers to pick one plan for all employees or let employees shop from a range of plans. A successful conversion of remaining Health Connector small group members on the former SHOP platform occurred in July 2018.

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The Financial Statements

The Health Connector's financial report includes three financial statements: the Statement of Net Position (similar to a balance sheet); the Statement of Revenues, Expenses and Changes in Net Position; and the Statement of Cash Flows. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the GASB. Under this method of accounting, an economic resources measurement focus and an accrual basis of accounting is used, similar to private industry. Revenue is recorded when earned, and expenses are recorded when incurred.

The Statement of Net Position presents information on the Health Connector's Total Assets and Deferred Outflows and Total Liabilities and Deferred Inflows, with the difference between the two reported as Net Position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Health Connector is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Position reports the operating revenues and expenses and nonoperating revenues and expenses of the Health Connector for the fiscal year. The difference – increase or decrease in net position – is presented as the change in net position for the fiscal year. The cumulative differences from inception forward are presented as the net position of the Health Connector, reconciling to total net position on the Statement of Net Position.

The Statement of Cash Flows presents information showing how the Health Connector's cash and cash equivalents position changed during the fiscal year. The Statement of Cash Flows classifies cash receipts and cash payments as resulting from operating activities, capital and related financing activities, noncapital financing activities and investing activities. The net result of those activities is reconciled to the cash and short-term investment balances reported at the end of the fiscal year. This statement is prepared using the direct method, which allows the reader to easily understand the amount of cash received and how much cash was disbursed.

Summarized Financial Information

Summarized financial information as of and for the years ended June 30, 2018 and 2017 is as follows:

Table 1

Net Position

(In thousands)

	<u>2018</u>	<u>2017</u>
Current assets	\$ 88,618	220,950
Capital assets	<u>246</u>	<u>356</u>
Total assets and deferred outflows	<u>\$ 88,864</u>	<u>221,306</u>

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June 30, 2018

Table 1
Net Position
(In thousands)

	<u>2018</u>	<u>2017</u>
Current liabilities	\$ 58,384	198,495
Long term liabilities	5,602	5,224
Deferred inflows of resources	3,446	—
Total liabilities and deferred inflows	<u>\$ 67,432</u>	<u>203,719</u>
Net position:		
Invested in capital assets	\$ 246	356
Unrestricted	21,186	17,231
Total net position	<u>\$ 21,432</u>	<u>17,587</u>

Table 2
Changes in Net Position
(In thousands)

	<u>2018</u>	<u>2017</u>
Operating revenues	\$ 746,057	626,004
Operating expenses	789,356	678,331
Operating loss	(43,299)	(52,327)
Nonoperating revenue	49,780	50,286
(Decrease) increase in net position	<u>\$ 6,481</u>	<u>(2,041)</u>

Financial Highlights

For FY2018, the Health Connector had a net operating loss of \$43,299,187 on operating revenues of \$746,057,081 and operating expenses of \$789,356,268.

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June 30, 2018

Operating revenues include \$440,402,076 in premiums billed to QHP and QDP enrollees. Premiums for QHP and QDP enrollees are billed one month in advance of the coverage period. Premium payments collected by the Health Connector from QHP and QDP enrollees are paid to the carriers on a monthly basis. Additional FY2018 operating revenues include state-funded premium subsidies and cost sharing reduction subsidies, which were \$128,506,283 and \$112,571,487, respectively. Both subsidies, which are part of the Health Connector's ConnectorCare program, supplement federal subsidies to further strengthen affordability of coverage for individuals with income at or below 300% of the FPL. These subsidies, which are funded from the Commonwealth Care Trust Fund (CCTF), are paid to the carriers on a monthly basis. The CCTF is a fund that is managed and administered by the Commonwealth.

FY 2018 operating revenue also includes \$5,304,737 in premiums billed to Health Connector for Business (HCB) employers. Premiums for HCB employers are billed one month in advance of the coverage period. Premium payments collected by the Health Connector from HCB employers are paid to the carriers on a monthly basis.

Additional FY2018 operating revenue includes \$30,656,967, of administrative fees assessed to the carriers. The administrative fee assessed to the carriers for ConnectorCare QHP enrollees is 3.0% of the sum of enrollee premiums paid, federal APTC and state premium subsidies paid to the carriers. The administrative fee assessed to the carriers for non-ConnectorCare QHP enrollees is 2.5% of the sum of enrollee premiums paid and federal APTC. The administrative fee assessed to the carriers for QDP enrollees is 3.0% of the enrollee premiums paid. Nonoperating revenue, includes federal grant revenue of \$2,311,492, a CCTF contribution for administrative operations of \$45,000,000, intergovernmental revenue of \$1,932,432 and investment income of \$532,216.

Contacting the Health Connector's Management

This financial report is designed to provide citizens, taxpayers and creditors with a general view of the Health Connector's finances and to show the Health Connector's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact Kari Miller, Chief Financial Officer, Commonwealth Health Insurance Connector Authority at 100 City Hall Plaza, 6th Floor, Boston, MA 02108

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Statement of Net Position

June 30, 2018

Assets and deferred outflows:	
Current assets:	
Cash and short-term investments (note 2)	\$ 59,938,175
Accounts receivable:	
Qualified Health and Dental plan enrollees, net (note 3)	8,452,980
Nonfederal grants	3,825
Due from Commonwealth (note 5)	16,693,057
Carriers (note 6)	3,261,254
Other assets	<u>268,919</u>
Total current assets	88,618,210
Noncurrent assets (note 10)	<u>246,240</u>
Total assets and deferred outflows	<u><u>\$ 88,864,450</u></u>
Liabilities and deferred inflows:	
Current liabilities:	
Accounts payable	\$ 5,288,215
Unearned revenue (note 4)	39,645,159
Accrued salary and benefits	647,133
Accounts payable – enrollee overpayments	8,736,667
Other liabilities	<u>4,066,806</u>
Total current liabilities	<u>58,383,980</u>
Long term liabilities:	
OPEB obligation (note 8)	<u>5,601,661</u>
Total long term liabilities	<u>5,601,661</u>
Deferred inflows of resources:	
Deferred inflows related to OPEB	<u>3,446,363</u>
Total deferred inflows of resources	<u>3,446,363</u>
Total liabilities and deferred inflows	<u><u>\$ 67,432,004</u></u>
Net position:	
Invested in capital assets	\$ 246,240
Unrestricted	21,186,206
Commitments and contingencies (note 9, 12 and 13)	
Total net position	<u><u>\$ 21,432,446</u></u>

See accompanying notes to financial statements.

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Statement of Revenues, Expenses, and Changes in Net Position

Year ended June 30, 2018

Operating revenues:	
Qualified health and dental plan enrollee premiums	\$ 440,402,076
Health Connector for Business enrollee premiums	5,304,727
State wrap premium subsidy – ConnectorCare	128,506,283
State cost sharing reduction subsidy – ConnectorCare	112,571,487
State Mandated Benefits	402,556
State funded federal replacement cost sharing reduction subsidy	27,363,630
Carrier Administrative fees	30,656,967
Risk adjustment data validation user fee	583,771
Other revenue	<u>265,584</u>
Total operating revenues	<u>746,057,081</u>
Operating expenses:	
Carrier payments – qualified health and dental plan enrollee premiums	440,402,076
Carrier payments – Health Connector for Business enrollee premiums	5,304,727
State wrap premium subsidy – ConnectorCare	128,506,283
State cost sharing reduction subsidy – ConnectorCare	112,571,487
State Mandated Benefits	402,556
State funded federal replacement cost sharing reduction subsidy (note 11)	27,363,630
Consulting and professional support	4,711,141
Customer service and premium billing	43,959,435
Navigator program	1,585,321
Salaries, benefits, and payroll taxes	7,699,688
Communications	2,203,648
General and administrative	458,280
IT and communications	9,706,776
Facility and related	897,029
Depreciation expense	109,685
Program appeals	194,393
Postemployment expense (notes 7 and 8)	3,121,539
Other expense	<u>158,574</u>
Total operating expenses	<u>789,356,268</u>
Operating loss	<u>(43,299,187)</u>
Nonoperating revenue:	
Federal grant revenue	2,311,492
CCTF contributions	45,000,000
Intergovernmental revenue (note 7)	1,932,432
Investment income	532,216
Other grant revenue	<u>3,825</u>
Total nonoperating revenue	<u>49,779,965</u>
Increase in net position	6,480,778
Net position – beginning of fiscal year, as restated	<u>14,951,668</u>
Net position – end of fiscal year	<u>\$ 21,432,446</u>

See accompanying notes to financial statements.

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Statement of Cash Flows

Year ended June 30, 2018

Cash flows from operating activities:	
Cash paid to employees	\$ (4,296,261)
Cash paid to vendors	(64,349,197)
Cash refunds paid due to enrollee overpayments	(11,200,856)
Cash received from Commonwealth	267,069,342
Cash paid to carriers	(707,728,856)
Cash paid to carriers (HCB)	(4,963,535)
Cash received from qualified health and dental plan enrollees	447,171,317
Cash received from Health Connector for Business enrollees	6,676,921
Cash refunds paid due to Health Connector Business enrollee overpayments	(54,311)
Cash received from health plans (MLR rebates)	6,569,294
Cash paid to Commonwealth (MLR rebates)	(6,569,294)
Cash paid to carriers (ACA Risk Adjustment)	(135,272,853)
Cash received from carriers (ACA Risk Adjustment)	135,272,853
Interest received	24,821
Operating revenue:	
Administrative fees	30,662,933
RADV user fee	4,250
Other	292,812
	<u>(40,690,620)</u>
Net cash used for operating activities	
Cash flows from capital and related financing activities:	
Cash received from federal grants	4,705,897
Cash received from Commonwealth (CCTF contributions)	44,429,971
	<u>49,135,868</u>
Net cash provided by capital and related financing activities	
Cash flow from investing activities:	
Investment earnings	532,216
	<u>532,216</u>
Net cash provided by investing activities	
Net increase in cash and short-term investments	
	8,977,464
Cash and short-term investments at the beginning of the fiscal year	<u>50,960,711</u>
Cash and short-term investments at the end of the fiscal year	<u>\$ 59,938,175</u>
Reconciliation of operating loss to cash used for operating activities:	
Operating loss	\$ (43,299,187)
Adjustments to reconcile operating loss to cash used for operating activities:	
Depreciation	109,685
Intergovernmental revenue	1,932,432
CCTF contributions	570,029
Decrease in nonfederal accounts receivable	137,981,011
Decrease in other assets	937,812
Decrease in accounts payable, and accrued liabilities	(140,111,509)
Increase in OPEB liability, net	1,189,107
	<u>1,189,107</u>
Net cash used for operating activities	<u>\$ (40,690,620)</u>

See accompanying notes to financial statements.

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Notes to Financial Statements

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(1) Summary of Significant Accounting Policies

(a) Reporting Entity

The Health Connector is an independent body politic and corporate and public health instrumentality of the Commonwealth of Massachusetts established pursuant to Chapter 176Q of the Massachusetts General Laws (MGLs) as added by Section 101 of Chapter 58 of the Acts of 2006.

Due to its relationship with the Commonwealth, the Health Connector is considered a discretely presented component unit and is presented as such in the Commonwealth's financial statements. The Health Connector has no relationship with other entities that could be considered component units.

(b) Basis of Presentation

The accompanying financial statements of the Health Connector have been prepared in accordance with U.S. GAAP, as prescribed by the Governmental Accounting Standards Board (GASB). The Health Connector has prepared a "Statement of Net Position," a "Statement of Revenues," "Expenses and Changes in Net Position" and a "Statement of Cash Flows," along with the required supplementary information titled "Management's Discussion and Analysis" which precedes the financial statements and the required supplementary schedules titled "Schedule of Proportionate Share of Net Pension Liability" and "Schedule of Changes in Total OPEB Liability and Related Ratios".

The Health Connector utilizes the full accrual basis of accounting, which focuses on changes in total economic resources, in the preparation of financial statements. Under the full accrual basis of accounting, long term assets and liabilities are reflected in the financial statements.

(c) Cash and Cash Equivalents

The Health Connector considers all highly liquid investments with an original maturity of 30 days or less when purchased to be cash equivalents.

(d) Investments

The Health Connector is authorized to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, bonds or notes of public agencies or municipalities, bank time deposits, guaranteed investment contracts, money market accounts, and repurchase agreements. These investments are recorded at fair value. Investments consist entirely of amounts held in the Massachusetts Municipal Depository Trust (MMDT), an external investment pool overseen by the Massachusetts State Treasurer. MMDT is recorded at its Net Asset Value (NAV) which is valued at \$1.00 per share as of June 30, 2018.

(e) Capital Assets

The Health Connector defines capital assets as classes of assets with an initial aggregate cost of more than \$49,999 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed.

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(f) Depreciation

Depreciation is calculated on the straight-line method based on the estimated useful lives of between three and 10 years for the applicable assets beginning in the fiscal year of acquisition.

(g) Revenue Recognition

The Health Connector recognizes revenue when earned. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

The Health Connector's major revenue sources are Qualified Health Plan (QHP) and Qualified Dental Plan (QDP) enrollee contributions, ConnectorCare state wrap premium and cost sharing reduction subsidies, and administrative fees collected from the carriers. The Health Connector's nonoperating revenue includes federal grant revenue, contributions from the CCTF, intergovernmental revenue, and investment income.

Operating revenues include premiums billed to QHP and QDP enrollees, state-funded premium wrap and cost sharing reduction subsidies. The state wrap and cost sharing reduction subsidies, which are part of the Health Connector's ConnectorCare program, supplement federal subsidies to further strengthen affordability of coverage for individuals with income at or below 300% of the FPL. Additional revenue is generated through administrative fees assessed to the carriers.

Federal grant revenue, intergovernmental revenue and investment income are reported as nonoperating revenues. Also reported in nonoperating revenues are contributions from the Commonwealth Care Trust Fund (CCTF) to support the Health Connector's operations.

Operating expenses include QHP and QDP enrollee premiums billed and collected by the Health Connector and paid to the carriers. Operating expenses also include state-funded premium and cost sharing reduction subsidies received from the CCTF and paid to the carriers. In addition, the Health Connector includes as operating expenses payments for customer service and business operations, the Navigator program, the Appeals program, outreach, personnel and other administrative items.

(h) Compensated Absences and Other Employee Benefits

Employees earn the right to be compensated during absences for vacation, personal and sick time (earned time or ET). Upon retirement, termination or death, certain employees are compensated for ET (subject to certain limitations) at their then current rate of pay. Accumulated ET is recorded as an expense and liability as benefits accrue. As of June 30, 2018, the ET liability was \$506,098.

The employees of the Health Connector participate in the Commonwealth's Group Insurance Commission (GIC) for all healthcare benefits except for dental and vision benefits, which are purchased directly through Delta Dental and Vision Service Plan.

(i) Use of Estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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June 30, 2018

(j) *Deferred Outflows of Resources and Deferred Inflows of Resources*

Deferred outflows of resources are defined as a consumption of net assets that is applicable to a future reporting period. Deferred inflows of resources are defined as an acquisition of net assets that is applicable to a future reporting period. Deferred outflows of resources increase net position, similar to assets, whereas deferred inflows of resources decrease net position, similar to liabilities.

(k) *Retirement Plan*

For purposes of measuring the net pension liability and pension expense, information about the fiduciary net position of the Massachusetts State Employees Retirement System (SERS) and additions to/deductions from SERS's fiduciary net position have been determined on the same basis as they are reported by SERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investment of assets in the SERS is with the Pension Reserves Investment Trust (PRIT) Fund, which is managed by the Pension Reserves Investment Management (PRIM) Board. The PRIM Board seeks to maximize the total return on investments within acceptable levels of risk for public pension funds. Investments are reported at fair value as described in the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Massachusetts.

(l) *Restatement of Net Position*

As a result of adopting GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, the net position as of July 1, 2017 was restated as follows:

Beginning net position as previously reported	\$ 17,586,872
Implementation of GASB 75	(2,635,204)
	14,951,668
Beginning net position, as restated	\$ 14,951,668

(2) Cash and Investments

(a) *Deposits with Financial Institutions*

Custodial credit risk is the risk that, in the event of the failure of a depository financial institution, the depositor will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. Deposits are exposed to custodial credit risk if they are large uninsured deposits with no collateral agreements.

As of June 30, 2018, the Health Connector had bank deposits of \$42,179,293 that exceeded the Federal Deposit Insurance Corporation (FDIC) coverage of \$250,000.

(b) *Investments*

The Health Connector's investment policy is to ensure that cash is invested in a stable investment option with consistent and competitive yields. As of June 30, 2018, available cash is invested in the MMDT Cash Portfolio option.

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Notes to Financial Statements

June 30, 2018

MMDT's average maturity is less than a year and not-rated for risk purposes. The Health Connector's position in MMDT as of June 30, 2018 was \$17,762,217. The unrestricted portion of the MMDT investment account funds operating accounts with other financial institutions and is classified as part of cash and short-term investments.

(3) Accounts Receivable – Qualified Health and Dental Plan Enrollees

As of June 30, 2018, the unpaid portion of the health insurance premium billed to QHP and QDP enrollees was \$16,566,189. The allowance for uncollectible accounts receivable at June 30, 2018 was \$8,113,209.

(4) Unearned Revenue

As of June 30, 2018, the Health Connector had \$39,645,159 in unearned revenue for QHP and QDP enrollees whose premiums are billed one month in advance of the coverage month.

(5) Due from Commonwealth

As of June 30, 2018, the amount due from the Commonwealth was \$16,693,057. The FY2018 amount due from the Commonwealth includes \$21,054,338 in state premium and cost sharing reduction subsidies and state mandated benefits paid by the Health Connector to the carriers in June 2018, and an unpaid June 2018 CCTF contribution of \$3,750,000. The amounts due from the Commonwealth are offset by \$8,808,100 which represents the Health Connector's share of the Health Insurance Exchange Integrated Eligibility System (HIX-IES) operations and maintenance costs incurred under the Optum contract, managed by MassIT.

(6) Accounts Receivable – Carriers

As of June 30, 2018, the amount due from the carriers was \$3,261,254 which represents QHP and QDP subscriber premium payments previously paid to the carriers and owed to the Health Connector.

(7) Retirement Plan

(a) Plan Description

All eligible employees of the Health Connector are provided with pension benefits through the Massachusetts SERS, a cost-sharing multiple-employer defined benefit pension plan administered by the Massachusetts State Retirement Board. SERS does not issue a stand-alone publicly available financial report, but its activities are included in a pension trust fund in the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Massachusetts.

(b) Benefits Provided

SERS provides retirement, disability, survivor and death benefits to members and their beneficiaries. The MGLs establishes the benefit and contribution requirements for SERS. These requirements provide for superannuation retirement allowance benefits up to a maximum of 80% of a member's highest three-year average annual rate of regular compensation. For employees hired after April 1, 2012, retirement allowances are calculated on the basis of the last five years of consecutive years, whichever is greater in terms of compensation. Benefit payments are based upon a member's age, length of creditable service, group creditable service, and group classification. The authority for amending these provisions rests with the Legislature.

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Members become vested after ten years of creditable service. A superannuation retirement allowance may be received upon the completion of twenty years of service or upon reaching the age of 55 with ten years of service. Normal retirement for most employees occurs at the age of 65; for certain hazardous duty and public safety positions, normal retirement is at the age of 55. Most employees who joined the system after April 1, 2012 cannot retire prior to age 60. The retirement systems' funding policies have been established by Chapter 32 of the MGL. The Legislature has the authority to amend these policies. The annuity portion of the SERS retirement allowance is funded by employees, who contribute a percentage of their regular compensation. Costs of administering the plan are funded out of plan assets.

(c) Contributions

SERS funding policies have been established by Chapter 32 of the MGL. The Legislature has the authority to amend these policies. Member contributions for SERS vary depending on the most recent date of membership from 5% regular compensation for hires prior to 1975 to 11% of regular compensation for hire dates after July 1, 2001. For members hired after 1979, an additional contribution of 2% of regular compensation in excess of \$30,000 is also required.

(i) Pension Liabilities and Pension Expense

At June 30, 2018, the Health Connector was allocated a liability of \$14,934,603 for its proportionate share of the net pension liability of SERS but was not required to record this liability as the Commonwealth is legally responsible for paying the liability.

The Commonwealth is legally responsible to make employer contributions related to the Health Connector's employees participating in SERS. As such, the Commonwealth has a 100% special funding situation for the Health Connector. Accordingly, the Health Connector recognized \$1,932,432 as pension expense and intergovernmental revenue of the same amount in the statement of revenues, expenses and changes in net position for the year ended June 30, 2018.

Health Connector's proportionate share of the net pension liability	\$	—
Commonwealth's proportionate share for the net pension liability associated with the Health Connector		14,934,603
Total	\$	14,934,603

The net pension liability was measured as of June 30, 2017 (the Measurement Date), and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of January 1, 2017 and rolled forward to the Measurement Date. The Health Connector's proportion of the net pension liability was based on allocated nonemployer contributions. At June 30, 2017, the Health Connector's proportion was 0.11645% which was an increase of 1.8% from its proportion of 0.11441% measured as of June 30, 2016.

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(d) Actuarial Assumptions

The total pension liability in the January 1, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement.

- Salary increases: 4.0% to 9.0% depending on the group and length of service
- Investment rate of return: 7.5% net of pension plan investment expense, including inflation; 3.5% interest rate credited to the annuity savings fund
- Cost of living increase: 3.0% per year

Mortality rates were based on the following:

- Pre-retirement – reflects RP 2014 Blue Collar Employees Table projected generationally with Scale MP-2016 and set forward 1 year for females
- Post-retirement – reflects RP 2014 Blue Collar Healthy Annuitant and table projected generationally with Scale MP-2016 set forward 1 year for females
- Disability – the mortality rate is assumed to be in accordance with the RP-2000 Healthy Annuitant Table projected generationally with Scale BB and a base year of 2015 (gender distinct)

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future rates of return by the target asset allocation percentage. Best estimates of geometric rates of return for each major asset class included in the Pension Reserve Investment Trust (PRIT) Fund's target allocation as of June 30, 2017 are summarized in the following table:

Asset class	Target allocation	Long term expected real rate of return
Core fixed income	12 %	1.1 %
Value added fixed income	10	3.8
Global equity	40	5.0
Real estate	10	3.6
Private equity	11	6.6
Hedge funds	—	3.6
Portfolio Completion Strategies	13	3.6
Timber/natural resources	4	3.2
Total	100 %	

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(e) Discount Rate

The discount rate used to measure the total pension liability was 7.5%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that contributions will be made at contractually required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

(i) Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in the Commonwealth's financial report.

(8) Other Post-Employment Benefits (OPEB)

(a) Plan Description

The Health Connector administers a single-employer defined benefit OPEB plan. The plan provides post-employment health care and life insurance benefits (OPEB) for eligible retired employees through the Group Insurance Commission (GIC). The GIC administers and manages health coverage options and benefits to participating employees and retirees. As of January 1, 2017, the date used for actuarial census data, the Health Connector had two retirees and 65 active employees who met the eligibility requirements. No assets are accumulated in a trust that meets the criteria of paragraph 4 of Statement No. 75.

(b) Benefits Provided

The Health Connector provides medical, dental, prescription drug, mental health/substance abuse and life insurance to retirees and their covered dependents. All active employees who retire from the Health Connector and meet the eligibility criteria will receive these benefits.

(c) Contributions

Employees who retire after July 1, 1994 but on or before October 1, 2009 contribute 15% of the cost of the health plan, as determined by the GIC. Employees who retire after October 1, 2009 contribute 20% of the cost of the plan as determined by the GIC. In both cases, the Health Connector contributes the remainder of the health plan costs on a pay-as-you-go basis.

(d) Total OPEB Liability

The Health Connectors' total OPEB liability of \$5,601,661 was measured as of June 30, 2017 and was determined by an actuarial valuation as of January 1, 2017 rolled forward to June 30, 2017.

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Actuarial Assumptions and Other Inputs

The total OPEB liability as of June 30, 2017 was determined using the following actuarial assumptions and other inputs, applied to all periods included in the measurement period:

Inflation	3.0 percent
Salary Increases	4.5 percent, average, including inflation
Healthcare cost trend rates	8.5 percent for 2017, decreasing 0.5 percent per year to an ultimate rate of 5.0 percent for 2024 and later years
Actuarial cost method	Entry age normal with 30 year open amortization period

Pre-retirement mortality reflects RP-2014 Blue Collar Employees table projected generationally with Scale MP-2016 set forward 1 year for females.

Post-retirement mortality reflects RP-2014 Blue Collar Healthy Annuitant table projected generationally with Scale MP-2016 set forward 1 year for females.

For disabled members, the mortality rate is assumed to be in accordance with the RP-2000 Healthy Annuitants projected generationally with Scale BB from 2015.

The actuarial assumptions used in the January 2017 valuation reflect the experience analysis published in 2014 (based on the years 2006–2011), updated to reflect actual experience from 2012 through 2016 for post-retirement mortality, and professional judgment. This assumption reflects observed current mortality as well as expected mortality improvement.

Discount Rate

The discount rate used to measure the total OPEB liability as of June 30, 2018 was 3.58%. The discount rate is based on the Bond Buyer General Obligation 20-year Municipal Bond Index, which includes tax-exempt general municipal bonds with an average rating of AA/Aa or higher.

Changes in Total OPEB Liability	
Balance at June 30, 2017	\$ 7,858,917
Changes for the year:	
Service cost	1,215,462
Interest on the total OPEB liability	258,534
Change of assumptions	(3,725,195)
Benefit payments	(6,057)
Net changes	<u>(2,257,256)</u>
Balance at June 30, 2018	<u>\$ 5,601,661</u>

Change of assumptions reflect a change in the discount rate from 2.85% to 3.58% in 2018.

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Sensitivity of the Total OPEB Liability to Changes in the Discount Rate and Healthcare Cost Trend Rates

The following table presents the total OPEB liability of the Health Connector, as well as what the Health Connector's total OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (2.58%) or 1 –percentage-point higher (4.58%) than the current discount rate:

	1% Decrease (2.58%)	Discount rate (3.58%)	1% Increase (4.58%)
Total OPEB liability	\$ 7,136,563	5,601,661	4,441,055

The following table presents the total OPEB liability of the Health Connector, as well as what the Health Connector's total OPEB liability would be if it were calculated using healthcare cost trend rates that are 1-percentage-point lower or 1 –percentage-point higher than the current healthcare cost trend rates:

	(7.5% decreasing to 4.0%) 1% decrease	Current healthcare cost trend rate – 8.5% decreasing to 5.0%	(9.5% decreasing to 6.0%) 1% increase
Total OPEB liability	\$ 4,085,460	5,601,661	7,851,199

(e) OPEB Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

For the year ended June 30, 2018, the Health Connector recognized OPEB expense of \$1,189,107. As of June 30, 2018, the Health Connector reported deferred inflows of resources of \$3,446,363 related to assumption changes.

Amounts recognized in the deferred inflows of resources related to OPEB will be recognized in the OPEB expense as follows:

Year end June 30:		
2019	\$	(278,832)
2020		(278,832)
2021		(278,832)
2022		(278,832)
2023		(278,832)
Total thereafter		<u>(2,052,203)</u>
	\$	<u><u>(3,446,363)</u></u>

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(9) Operating Lease

The Health Connector has an operating lease for office space on three floors at 100 City Hall Plaza. The lease terminates on August 30, 2021. Future minimum operating lease payments at June 30, 2018 are as follows:

Fiscal year:			
2019		\$	704,253
2020			723,373
2021			742,493
2022			124,280
			124,280
		\$	2,294,399

During FY2018, the amount of operating lease payments was \$685,133. During FY2017, the amount of operating lease payments was \$657,717.

(10) Capital Assets

Capital assets as of June 30, 2018 are as follows:

	Beginning balance <u>June 30, 2017</u>	Increases/ decreases	Ending balance <u>June 30, 2018</u>
Capital assets:			
Computers and equipment	\$ 102,484	—	102,484
Furniture and fixtures	267,669	—	267,669
Computer software	813,738	—	813,738
Total capital assets	1,183,891	—	1,183,891
Less accumulated depreciation:			
Computers and equipment	(68,472)	(14,641)	(83,113)
Furniture and fixtures	(261,175)	(4,924)	(266,099)
Computer software	(498,319)	(90,120)	(588,439)
Total accumulated depreciation	(827,966)	(109,685)	(937,651)
Total capital assets, net	\$ 355,925	(109,685)	246,240

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(11) State Funded Federal Replacement Cost Sharing Reduction Subsidy

In October 2017, the federal government discontinued federal cost sharing reduction subsidy payments to the carriers for subsidized individuals as of September 2017. In an effort to ease the burden on the carriers, the Commonwealth made the decision to make state funded federal replacement cost sharing reduction subsidy payments to the carriers for the period October 2017 through December 2017. These state funded payments were based on monthly premium data and will be subject to reconciliation based on the final actual claims data submitted by the carriers in 2018.

(12) Commitments and Contingencies

In February 2015, the Health Connector received a grand jury subpoena from the U.S. Attorney's Office of the District of Massachusetts seeking documents regarding the development of an electronic health insurance exchange and integrated eligibility system by the Commonwealth and the private vendors involved in that project. It has been publicly reported that other state entities involved in the project have received a similar subpoena. At this time, the Health Connector has responded to the subpoena by providing documents and information. The Health Connector is unable to predict the outcome or time frame of this subpoena or any related investigation.

Other than the foregoing, the Health Connector is not currently involved in any pending legal actions arising in the normal course of activities.

The Health Connector receives financial assistance from the Federal government principally in the form of grants primarily for one-time, ACA transition activities. As a grant recipient, the Health Connector is responsible for compliance with terms and conditions of grant agreements and applicable Federal regulations, including the expenditure of resources for eligible purposes. All Federal grants received by the Health Connector are subject to audit under the requirements of the Federal Single Audit Act. During FY2018, the Health Connector incurred expenditures related to the implementation of the ACA. The spending was primarily for period costs, contractual services and internal costs related to the implementation.

(13) HIX-IES Project

As of May 1, 2014, the Commonwealth's IT department, Mass IT has contracted with Optum to develop a HIX-IES. That contract is still active, and development work on the HIX-IES is ongoing. As a user of the HIX-IES, the Health Connector is obligated to provide a portion of the development costs of the HIX-IES, along with the state's Medicaid agency, which is the other user of the system. The Health Connector's share of the costs have been developed per the project's approved cost allocation methodology. The Health Connector's share of the costs are funded by Exchange Establishment grants or the Early Innovator grant (administered by the University of Massachusetts Medical School). HIX-IES operations and maintenance costs allocated to the Exchange are funded by the Health Connector with nonfederal funds and paid to Mass IT in the form of a chargeback under an Interagency Service Agreement (ISA).

As of FY2018, the Health Connector has included \$8,808,100 in Due from Commonwealth in the accompanying financial statements for the estimated share of the costs due to Mass IT.

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(14) Group Market Exchange (GME) Health Care for Business (HCB)

In March 2017, the Health Connector entered into a partnership with the District of Columbia Health Benefits Exchange (DCHBX) to develop a new Health Care for Business (HCB) program Group Market Exchange to offer coverage to small businesses with fewer than 50 employees. The GME HCB program began operations on August 15, 2017. In FY2018, the Health Connector incurred \$5,029,883 in costs, in which \$2,010,927 were implementation costs that were funded by a Federal Establishment Grant awarded to the Health Connector for \$9.7 million.

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Schedule of Proportionate Share of Net Pension Liability
Required Supplementary Information

June 30, 2018

(Unaudited)

	2018 (measurement date June 30, 2017)	2017 (measurement date June 30, 2016)	2016 (measurement date June 30, 2015)
Health Connector's proportion of the net pension liability	0.11645 %	0.11441 %	0.10439 %
Health Connector's share of the net pension liability	\$ —	—	—
State's proportionate share of the net pension liability associated with the Health Connector	<u>14,934,603</u>	<u>15,775,710</u>	<u>11,882,332</u>
Total net pension liability	<u>\$ 14,934,603</u>	<u>15,775,710</u>	<u>11,882,332</u>
Health Connector's covered-employee payroll	\$ 6,649,289	6,286,232	5,860,359
Health Connector's proportionate share of the net pension liability as a percentage of its covered-employee payroll	— %	— %	— %
Plan fiduciary net position as a percentage of the total pension liability	67.21 %	63.50 %	67.90 %

The Health Connector is not required to make contributions to the State Employees Retirement System.

Accordingly, the RSI related to statutorily or contractually contributions is not presented.

Note: This schedule is intended to present 10 years of data. Additional years will be presented when available.

See accompanying independent auditors' report.

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Schedule of Changes in Total OPEB Liability and Related Ratios
Required Supplementary Information

June 30, 2018

(Unaudited)

	2018 (measurement date June 30, 2017
Total OPEB liability:	
Service cost	\$ 1,215,462
Interest on the total OPEB liability	258,534
Change of assumptions	(3,725,195)
Benefit payments	<u>(6,057)</u>
Net change in total liability	(2,257,256)
Total OPEB liability – beginning	<u>7,858,917</u>
Total OPEB liability – ending	\$ <u><u>5,601,661</u></u>
Fiduciary net position as a percentage of OPEB liability	\$ —
Covered-employee payroll	6,649,289
Net OPEB liability as a percentage of covered-employee payroll	84 %

Notes to schedule:

Changes in Assumptions: the discount rate was changed from 2.85% as of the June 30, 2016 measurement date to 3.58% as of the June 30, 2017 measurement date.

Note: This schedule is intended to present 10 years of data. Additional years will be presented when available.

See accompanying independent auditors' report.