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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Oregon Health Insurance Exchange Corporation
Portland, Oregon

We have audited the accompanying financial statements of Oregon Health Insurance Exchange Corporation (the Exchange), as of December 31, 2011 and for the period from inception (September 1, 2011) to December 31, 2011, which collectively comprise the Exchange's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Exchange's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Oregon Health Insurance Exchange Corporation, as of December 31, 2011, and the respective changes in financial position, and, where applicable, cash flows thereof for the period then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 9, 2012, on our consideration of the Oregon Health Insurance Exchange Corporation'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* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on page 3 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.

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Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Oregon Health Insurance Exchange Corporation's basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements. The schedule of expenditures of federal awards is the responsibility of management and was derived from and relate 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 basic 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 basic financial statements as a whole.

AKT LLP

Salem, Oregon
April 9, 2012

THE OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Management's Discussion and Analysis

September 1, 2011 (inception) to December 31, 2011

The Oregon Health Insurance Exchange Corporation (the Exchange) financial statements – including the Balance Sheet; the Statement of Revenues, Expenses, and Changes in Fund Equity; and the Statement of Cash Flows -- are designed to provide an overview of the Exchange's financial position and activities. Management prepares this Discussion and Analysis to assist the reader of these financial statements.

In June 2011 the Oregon Legislature passed Senate Bill (SB) 99, creating the Exchange as a public corporation to implement a central marketplace for individuals and small employers to shop for health insurance and access federal tax credits pursuant the Federal Patient Protection and Affordable Care Act (ACA) of 2010. There is no state funding for the Exchange. Federal grants will fund start-up costs and the first year of operations, 2014. SB 99 allows the Exchange to assess participating insurance carriers an administrative fee, based on a percentage of earned premium for enrollees in the Exchange plans, to cover its operating costs and to build an operating reserve. In 2015, the Exchange must be financially self-sustaining through this assessment.

Financial Statements

The Exchange began operations in September 2011. Prior to this date, and in anticipation of SB 99, the Oregon Health Authority (OHA) began to research and plan for the formation of the Exchange with a \$1 million federal grant. Upon incorporation, OHA advanced the Exchange \$250,000 to fund initial operations. This advance was increased to \$499,000 in October 2011. Meanwhile, the Exchange secured an initial "Level 1" federal grant of \$8.9 million to cover start-up activities through August 2012. The federal grant is funded monthly upon the Exchange's submission of an invoice for costs incurred. The Exchange is preparing for the submission of the "Level 2" grant to fund operations through 2014.

As shown in the attached Statement of Revenues, Expenses and Changes in Fund Equity, \$1.1 million in federal grant revenue was recognized in the four-month-period ended December 31, 2011. The Exchange incurred operating expenses of approximately \$997,000, 90 percent of which were for staff salaries and benefits, and consulting expenses. Approximately \$90,000 was incurred for the acquisition of IT equipment and leasehold improvements (see the Statement of Cash Flows and Footnote 3).

The Balance Sheet shows that the Exchange has \$555,000 in cash and a \$107,000 receivable from the federal grant as of December 31, 2011. Accounts payable and payroll liabilities for incurred but unpaid operating expenses were \$141,000 and \$21,000, respectively. Fund equity, representing the net book value of funds invested in capital assets stands at \$85,000.

The notes attached to the financial statements provide the reader with several important disclosures, including a summary of the significant accounting practices used by the Exchange. A comparative analysis will be provided in future years when prior year information is available.

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Balance Sheet

December 31, 2011

ASSETS

Current assets:

Cash	\$ 555,172
Federal grants receivable	<u>106,563</u>

Total Current Assets 661,735

Capital assets:

Leasehold improvements	23,138
Furniture and equipment	<u>66,392</u>
	89,530
Less accumulated depreciation	<u>(4,037)</u>

Capital assets, net 85,493

Total Assets \$ 747,228

LIABILITIES AND FUND EQUITY

Current liabilities:

Accounts payable	\$ 141,433
Payroll liabilities	<u>21,302</u>

Total Current Liabilities 162,735

Noncurrent liabilities:

Interagency advance	<u>499,000</u>
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Total Liabilities 661,735

Fund equity:

Invested in capital assets	<u>85,493</u>
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Total Liabilities and Fund Equity \$ 747,228

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Statement of Revenues, Expenses, and Changes in Fund Equity

Inception (September 1, 2011) to December 31, 2011

Operating Revenues:

Federal grants \$ 1,082,036

Operating Expenses:

Salaries, payroll taxes, and benefits 761,890

Professional services 140,995

Equipment and supplies 42,227

Occupancy 23,957

Travel 13,690

Depreciation and other 13,784

Total Operating Expenses 996,543

Increase in Fund Equity 85,493

Fund Equity - Beginning of Period -

Fund Equity - End of Period \$ 85,493

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Statement of Cash Flows

Inception (September 1, 2011) to December 31, 2011

Cash Flows from Operating Activities:

Federal grants received	\$ 975,473
Cash paid for materials and services	(89,183)
Cash paid to employees and for taxes and benefits	<u>(740,588)</u>
Net Cash Provided by Operating Activities	<u>145,702</u>

Cash Flows from Capital and Related Financing Activities:

Acquisition of capital assets	(89,530)
Proceeds from intergovernmental agreement	<u>499,000</u>
Net Cash Provided by Capital and Related Financing Activities	<u>409,470</u>

Net Increase in Cash 555,172

Cash - Beginning -

Cash - Ending \$ 555,172

Reconciliation of Increase in Fund Equity to Net

Cash Provided by Operating Activities:

Increase in fund equity	\$ 85,493
Adjustments to reconcile increase in fund equity income to net cash provided by operating activities	
Depreciation	4,037
Changes in assets and liabilities:	
Accounts receivable	(106,563)
Accounts payable	141,433
Payroll liabilities	<u>21,302</u>

Net Cash Provided by
Operating Activities \$ 145,702

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Notes to Financial Statements

Inception (September 1, 2011) to December 31, 2011

Note 1 - Description of the Business & Regulatory Environment

The Oregon Health Insurance Exchange Corporation (the Exchange) is a central marketplace where consumers and small employers can shop for health insurance plans and find help paying for coverage. Starting in October of 2013 (for coverage effective January 2014), Oregonians will be able to easily compare plans, find out if they are eligible for tax credits and other financial assistance, and enroll for health insurance coverage through the Exchange website. In 2011, the Oregon Legislature passed Senate Bill 99 which created a public corporation to operate the Exchange in the public interest for the benefit of the people and businesses that obtain health insurance coverage for themselves, their families, and their employees through the Exchange. The Exchange began operations in September 2011. The Exchange is governed by a Board of Directors whose members are appointed by the Governor and confirmed by the Senate. Although independent of state government, the Exchange is required to provide regular updates to the Oregon legislature and meets regularly with a Legislative Oversight Committee.

Federal grant funding finances the start-up phase and the first year of operations, 2014. In 2015, the Exchange must be financially self-sustaining via administrative fee assessments on insurance plans sold through the Exchange. Senate Bill 99 sets a maximum fee of between 3 and 5 percent of earned premium depending on the enrollment. Because the Exchange will begin with zero enrollees, it will initially charge the maximum fee of 5 percent. The fee will adjust downward each year as enrollment grows. Senate Bill 99 further stipulates that revenue generated by the assessment in excess of what is necessary to fund operations will be used to build a six-month operating reserve. Any excess beyond that is required to be refunded to the participating insurance carriers.

Note 2 - Summary of Significant Accounting Policies

Basis of Accounting

The Exchange's financial statements are presented on the economic resources measurement focus and the accrual basis of accounting and conform to accounting principles generally accepted in the United States of America for proprietary (enterprise) funds. Accordingly, revenues are recorded when earned and expenses are recorded when a liability is incurred. The Exchange complies with all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as the Financial Accounting Standards Board (FASB) codification as applied on or before November 30, 1989, unless those contradict GASB pronouncements. In accordance with GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Fund Accounting, the Exchange only follows Statements of Financial Accounting Standards Board issues prior to November 30, 1989.

Cash

The Exchange maintains its cash either in bank deposit accounts that are insured by the Federal Deposit Insurance Corporation (FDIC) up to a limit of \$250,000 per depositor or in certain non-interest bearing accounts that are fully insured by the FDIC. Further, ORS 295 was established to provide a shared liability pool, increasing the protection to public funds, while allowing banks to pledge collateral more accurately reflecting their actual public funds deposited. As of December 31, 2011 the Exchange did not have any cash in any one bank that exceeded the FDIC limit due to the Public Funds Collateralization Program administered by the Oregon Office of the State Treasurer as the Exchange only deposits money in qualified depositories in order to meet the collateral requirements established by ORS 295.

The Exchange has not experienced any losses on such accounts and believes it is not exposed to any significant credit risk on cash.

For purposes of the statement of cash flows, the Exchange considers all highly liquid investments (including restricted assets) with a maturity when purchased of three months or less to be cash.

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Notes to Financial Statements

Inception (September 1, 2011) to December 31, 2011

Note 2 - Summary of Significant Accounting Policies, continued

Federal Grant Receivable

Federal Grant Receivable represents unreimbursed federal grant funds as of December 31, 2011 for the Level 1 Establishment Grant. Management believes this amount is fully collectible, as such no allowance for uncollectible receivables has been established. The total grant award is \$8,969,600 which expires in August 2012.

Fair Value of Financial Instruments

The Exchange's financial instruments, none of which are held for trading purposes, include cash, receivables, and accounts payable. The Exchange estimates that the fair value of all of these non-derivative financial instruments at December 31, 2011 does not differ materially from the aggregate carrying value of its financial instruments recorded in the accompanying balance sheet.

Capital Assets

Purchased capital assets are reported at cost. No estimates were made for historic costs and no assets were donated which would require an estimate of fair market value at the date received. The Exchange's capitalization levels are \$5,000 for tangible personal property and leasehold improvements. There are no acquisitions of land or other real property.

Costs of assets sold or retired (and related amounts of accumulated depreciation) are eliminated from the accounts in the year of sale or retirement, and the resulting gain or loss is included in the operating statement of the related fund. Other costs incurred for repairs and maintenance are expensed as incurred.

Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

	Years
Leasehold improvements	5
Furniture and equipment	3

Fund Equity

Fund equity comprises the various net earnings from operations, non-operating revenues, expenses and contributions of capital. Fund equity is classified in the following two categories:

- Invested in capital assets, net of related debt – consist of all capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds or other borrowings that are attributable to the acquisition, construction, or improvement of the assets. There were no such borrowings as of December 31, 2011.
- Unrestricted fund net assets – consist of all other fund net assets that are not included in the other categories previously mentioned. There were no unrestricted net assets at December 31, 2011.

Operating Revenue and Expense

The Exchange distinguishes operating revenues and expenses from non-operating items. Operating revenues include federal grant funds received. Operating expenses include all expenses directly and indirectly related to establishing and running a health exchange. There were no non-operating items in the period ended December 31, 2011.

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 under the State of Oregon's self-insurance and commercial insurance program, administered by the Department of Administrative Services, Risk Management Division.

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Notes to Financial Statements

Inception (September 1, 2011) to December 31, 2011

Note 2 - Summary of Significant Accounting Policies, continued

Estimates

The Exchange uses estimates and assumptions in preparing financial statements in accordance with accounting principles generally accepted in the United States of America. The preparation of the financial statements require management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported revenues and expenses during the reporting period. Actual results could differ from those estimates.

Subsequent Events

The Exchange has evaluated subsequent events through April 9, 2012, which is the date the financial statements were available to be issued.

Note 3 Capital Assets

Capital assets consisted of the following as of December 31, 2011:

	<u>Beginning of period</u>	<u>Additions</u>	<u>Retirements</u>	<u>End of period</u>
Leasehold improvements	\$ -	\$ 23,138	\$ -	\$ 23,138
IT equipment	-	66,392	-	66,392
Total capital assets	-	89,530	-	89,530
Accumulated depreciation	-	\$ 4,037	\$ -	4,037
Total capital assets, net	\$ -			\$ 85,493

Note 4 - Pension Plan

Defined Benefit Plan

Plan Description

The Exchange participates in the Oregon Public Employees Retirement System (PERS), an agent multiple-employer defined benefit pension plan and the Oregon Public Service Retirement Plan (OPSRP), an agent multiple-employer hybrid pension plan. Both PERS and OPSRP are governed by the Public Employees' Retirement Board (PERB) under the provisions of Oregon Revised Statutes 238. PERS provides benefits under a variety of benefit options, as selected by retiring employees, and provides death and disability benefits. OPSRP provides a combination of retirement benefits under a defined pension plan and individual account program (IAP), the balance of which will be paid out in either a lump sum or over a 5, 10, 15, or 20-year-period. Employees hired on or after August 29, 2003 participate only in OPSRP. Beginning January 1, 2004, active PERS members hired before August 29, 2003 became members of IAP of OPSRP. These members retain their existing PERS account, however any future member contributions will be placed in the OPSRP IAP. Exchange employees are eligible to participate after completing six months of service.

For the period ended December 31, 2011, the Exchange's total payroll for all employees and the Exchange's total covered payroll amounted to \$586,174. Covered payroll refers to all compensation paid by the Exchange to active employees and covered by PERS and OPSRP on which contributions are based.

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Notes to Financial Statements

Inception (September 1, 2011) to December 31, 2011

Note 4 - Retirement Plans, continued

Plan Description, continued

A copy of the Oregon Public Employees' Retirement System annual financial report may be obtained by writing to Public Employees' Retirement System, P.O. Box 23700, Tigard, OR 97281-3700, by calling (503) 598-7377 or at www.oregon.gov/PERS.

Funding Policy:

The Exchange contribution rate for members is set by state statute. Covered employees are required by state statutes to contribute 6% of their annual salary to the system. The Exchange has chosen to pay the employee contribution. The contribution rate for the Exchange is set by the PERB and is periodically changed based upon actuarial computations of the amount needed to adequately provide for benefits. The Exchange's 2011 contribution rate as a percentage of member salaries for PERS and OPSRP was 9.55% and 8.05%, respectively.

Annual Pension Cost:

Total contributions, including member and employer contributions, paid by the Exchange for 2011 were \$74,490. Annual pension costs have equaled the annual required contributions.

Employer contribution rates for the two-year-period ended June 30, 2013 are based on the actuarial valuation dated December 31, 2009. The fair market value method is used to determine the actuarial value of the plan's assets. The actuarial assumptions include:

- Investment return of 8%, net of investment expenses.
- Postretirement benefit increases of 2%.
- Projected salary increases of 3.75%.
- Inflation rate of 2.75%.

Employer contribution rates are set using the entry age actuarial cost method. This method produces an employer contribution rate consisting of:

- An amount for normal cost (the estimated amount necessary to finance benefits earned by the employees during the current service year).
- An amount for amortization of the unfunded actuarial accrued liability, if any, over a period of 30 years.
- An actuarially determined amount for funding post-employment healthcare subsidies.

An expected value of assets is projected using the assumed rate of investment yield, currently.

Deferred Compensation Plan

The Exchange has a deferred compensation plan (the Plan) created in accordance with the Internal Revenue Code Section 457, as amended. The Plan is administered by the independent plan administrators Oregon Savings Growth Program and ING. The Plan is available to all employees of the Exchange. Employees defer a portion of their salary until future years. Deferred compensation is not available to employees until termination, retirement, death, or financial hardship.

The Plan's assets are held in a custodial account for the exclusive benefit of participants and beneficiaries and are not subject to the claims of the Exchange's creditors, nor can they be used by the Exchange for any purpose other than the payments of benefits to the Plan's participants.

OREGON HEALTH INSURANCE EXCHANGE CORPORATION

Notes to Financial Statements

Inception (September 1, 2011) to December 31, 2011

Note 5 - Interagency Advance

In 2011 the Exchange entered into an intergovernmental agreement with the Oregon Health Authority to provide an advance of funds for initial operating and start-up costs prior to the receipt of federal grant funds. The initial agreement was amended in October 2011 increasing the amount of the advance to \$499,000. The entire amount of operating capital advanced under this agreement is due no later than June 30, 2013.

Note 6 - Leases

During 2011 the Exchange entered into two separate leases for office space in Portland and Salem. These leases vary in length from 17 to 60 months. Lease expenses for the period ended December 31, 2011, including amounts paid for real estate taxes, parking, and operating expenses, were \$22,649.

Future minimum payments under all operating leases are as follows:

Year ending December 31,	Amount
2012	\$ 198,003
2013	168,814
2014	165,993
2015	169,873
2016	159,052