
New Mexico Health Insurance Exchange

Albuquerque, New Mexico

*Financial Statements,
Independent Auditor's Report, and
Single Audit Reporting Package
December 31, 2014 and 2013*

New Mexico Health Insurance Exchange

Table of Contents

	<u>Page</u>
Independent Auditor’s Report	1-3
Management’s Discussion and Analysis	4-7
Financial Statements	
Statements of Net Position	8
Statements of Revenues, Expenses and Changes in Net Position	9
Statements of Cash Flows	10
Notes to the Financial Statements	11-22
Single Audit	
Schedule of Expenditures of Federal Awards	23
Notes to the Schedule of Expenditures of Federal Awards	24
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 <i>Government Auditing Standards</i>	25-26
Independent Auditor’s Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133	27-29
Schedule of Findings and Questioned Costs	30-39
Summary Schedule of Prior Audit Findings	40
Corrective Action Plan	41
Exit Conference	42

Independent Auditor's Report

Board of Directors
New Mexico Health Insurance Exchange

Report on the Financial Statements

We have audited the accompanying financial statements of the New Mexico Health Insurance Exchange (the "Exchange"), as of and for the year ended December 31, 2014, and as of December 31, 2013 and for the period from inception (April 28, 2013) through December 31, 2013, and the related notes to the financial statements, which collectively comprise the Exchange's basic 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 the accompanying 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 the accompanying 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 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 the Exchange as of December 31, 2014 and 2013, and the changes in financial position and cash flows thereof for the year ended December 31, 2014, and for the period ended December 31, 2013, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Exchange'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 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 relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such 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 basic financial statements or to the basic 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 28, 2015, 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.

REDW LLC

Albuquerque, New Mexico
August 28, 2015

Required Supplementary Information
Management's Discussion and Analysis

New Mexico Health Insurance Exchange

Management's Discussion and Analysis

December 31, 2014 and 2013

Introduction

This section of the financial report presents our discussion and analysis of the net position and changes in the net position of the New Mexico Health Insurance Exchange (the "Exchange") as of December 31, 2014, and for the year then ended, and as of December 31, 2013, and for the period from inception (April 28, 2013) through December 31, 2013. Please read this discussion and analysis in conjunction with the Exchange's financial statements, which follow this section.

The Exchange is a governmental entity organized pursuant to the New Mexico Health Insurance Exchange Act (the "Act") which replaces the New Mexico Health Insurance Alliance Act that was created by the State of New Mexico. The purpose of the Exchange is to provide qualified individuals and qualified employers with increased access to health insurance in the State.

Overview of the Financial Statements

The financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with generally accepted accounting principles. Accordingly, the Exchange presents the following three financial statements:

- The *Statements of Net Position* present information on the Exchange's assets and liabilities, with the differences between the assets and liabilities reported as net position. Over time, increases or decreases in net position serve as a useful indicator of whether the financial position of the Exchange is improving or deteriorating.
- The *Statements of Revenues, Expenses and Changes in Net Position* present information reflecting how net position changed during the year. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of timing of related cash flows. Thus, revenues and expenses are reported for some items that will only result in cash flows in future or prior periods.
- The *Statements of Cash Flows* present information showing how the Exchange's cash balances changed during the year. The cash flows are separately detailed for operating activities, investing activities, capital and related financing activities and noncapital financing activities.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes can be found immediately following the financial statements.

Financial Highlights

- The Exchange was awarded an additional establishment grant on January 22, 2014, in the amount of \$69.4 million for the continued development of the individual insurance marketplace exchange. During 2014, \$47.0 million was spent for operations and the continued development of the individual exchange.

New Mexico Health Insurance Exchange
Management's Discussion and Analysis
December 31, 2014 and 2013

- The Exchange's total assets were \$15.8 million and \$5.6 million as of December 31, 2014 and 2013, respectively, mainly consisting of cash, receivables from the U.S. Department of Health and Human Services, and capital assets.
- The Exchange's total liabilities were \$15.8 million and \$5.6 million as of December 31, 2014 and 2013, respectively, mainly consisting of accounts payable and contract holdbacks.
- The Exchange's total nonoperating revenues were \$47.0 million and \$22.3 million in 2014 and 2013, respectively, with grants from the federal government being the sole revenue source.
- The Exchange's total expenses were \$47.0 million and \$22.3 million in 2014 and 2013, respectively, which were related to establishing and operating the Exchange.

Statement of Net Position

The following shows condensed statements of net position as of December 31:

	2014	2013
Current assets	\$ 15,711,468	\$ 5,463,860
Noncurrent assets	107,462	133,992
Total assets	<u>\$ 15,818,930</u>	<u>\$ 5,597,852</u>
Current liabilities	<u>\$ 15,818,930</u>	<u>\$ 5,597,852</u>
Invested in capital assets	107,462	133,992
Unrestricted	<u>(107,462)</u>	<u>(133,992)</u>
Total net position	<u>-</u>	<u>-</u>
Total liabilities and net position	<u>\$ 15,818,930</u>	<u>\$ 5,597,852</u>

The \$10.2 million increase in current assets during 2014 is primarily due to the increase in grant receivables from the U.S. Department of Health and Human Services as a result of increased operating expenses. There was no change in net position for the Exchange in 2014.

New Mexico Health Insurance Exchange
Management's Discussion and Analysis
December 31, 2014 and 2013

Statement of Revenues, Expenses, and Changes in Net Position

The following shows condensed statements of revenues, expenses, and changes in net position for the year ended December 31, 2014 and for the period ended December 31, 2013:

	<u>2014</u>	<u>2013</u>
Total operating expenses	<u>\$ 47,014,645</u>	<u>\$ 22,330,809</u>
Operating loss	<u>(47,014,645)</u>	<u>(22,330,809)</u>
Total nonoperating revenues	<u>47,014,645</u>	<u>22,330,809</u>
Change in net position	-	-
Beginning net position	<u>-</u>	<u>-</u>
Total net position, year-end	<u>\$ -</u>	<u>\$ -</u>

The Exchange did not have operating revenue in 2014 and 2013. Total operating expenses were approximately \$47.0 million and \$22.3 million, resulting in an operating loss of the equivalent amounts. In 2014 and 2013, all of the Exchange's revenues were from federal grants. Because grant revenues are recognized based on qualifying expenses, nonoperating revenues also totaled \$47.0 million and \$22.3 million for the respective periods, resulting in no net position at the beginning and end of the periods.

The \$24.7 million increase in nonoperating revenues and operating expenses during 2014 is primarily due to recognizing a full operating years' worth of activity, as well as meeting several significant contract deliverables in establishing the individual insurance exchange.

Capital Assets

At December 31, 2014 and 2013, the Exchange had \$107,462 and \$133,992, respectively, net of accumulated depreciation, invested in capital assets, including furniture and fixtures, office equipment, computer software, and computer equipment. Additional information on the Exchange's capital assets can be found in Note 4 to the financial statements.

Economic Factors and Next Year's Budget

All of the Exchange's operating funding is obtained through grants from the federal government. The availability of funding from the federal government can fluctuate as a result of economic factors affecting the federal government. For the fiscal year 2015 operating budget, the Exchange adhered to a balanced budget that required all 2015 revenues to equal the budgeted operating and capital expenses. The budget was formulated based on the total available funding under the Exchange's 3rd Level 1 Establishment Grant, in addition to carrier assessments approved under the Exchange's Financial Sustainability Plan which was approved in December 2014. This Plan allows for market assessments for all major medical and Medicaid carriers in New Mexico.

New Mexico Health Insurance Exchange
Management's Discussion and Analysis
December 31, 2014 and 2013

The Small Employer Health Options Program (SHOP) marketplace was implemented effective January 1, 2014, and operating costs of the SHOP were funded through the grant funds for all of 2014. Beginning January 1, 2015, the SHOP is required to be financially sustainable for all ongoing maintenance and operating expenses.

Contacting the Exchange's Financial Management

This financial report is designed to provide the New Mexico Health Insurance Exchange and its customers with a general overview of the Exchange's finances and to show the Exchange's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact:

New Mexico Health Insurance Exchange
6301 Indian School Road NE, Suite 100
Albuquerque, New Mexico 87110
(505) 314-5211

Financial Statements

New Mexico Health Insurance Exchange
Statements of Net Position
December 31,

	2014	2013
Assets		
Current assets		
Cash	<u>\$ 1,066,178</u>	<u>\$ 874,869</u>
Receivables		
Due from U.S. Department of Health and Human Services	14,583,751	4,542,811
Premiums due	39,968	-
Due from New Mexico Health Insurance Alliance	-	26,849
Other receivables	<u>-</u>	<u>1,832</u>
Total receivables	14,623,719	4,571,492
Prepaid expenses and other assets	<u>21,571</u>	<u>17,499</u>
Total current assets	15,711,468	5,463,860
Noncurrent assets		
Capital assets, net of accumulated depreciation	<u>107,462</u>	<u>133,992</u>
Total assets	<u>\$ 15,818,930</u>	<u>\$ 5,597,852</u>
Liabilities		
Current liabilities		
Accounts payable	\$ 13,660,138	\$ 3,388,623
Due to carriers	156,467	1,074
Due to New Mexico Health Insurance Alliance	-	65,318
Contract holdback	1,932,777	-
Accrued payroll and related liabilities	20,020	6,636
Compensated absences	49,528	62,495
Unearned revenue	<u>-</u>	<u>2,073,706</u>
Total current liabilities	<u>15,818,930</u>	<u>5,597,852</u>
Net Position		
Net investment in capital assets	107,462	133,992
Unrestricted	<u>(107,462)</u>	<u>(133,992)</u>
Total net position	<u>-</u>	<u>-</u>
Total liabilities and net position	<u>\$ 15,818,930</u>	<u>\$ 5,597,852</u>

The accompanying notes are an integral part of the financial statements.

New Mexico Health Insurance Exchange
Statements of Revenues, Expenses and Changes in Net Position
For the Year Ended December 31, 2014 and
for the Period Ended December 31, 2013

	2014	2013
Operating Expenses		
Technology and project management	\$ 28,628,498	\$ 16,738,930
Consumer and stakeholder engagement and support	15,542,544	4,628,453
Salaries and employee benefits	1,666,426	409,139
Operations	465,034	283,909
Professional services and board	422,143	270,378
Plan management	275,000	-
Other	15,000	-
Total operating expenses	47,014,645	22,330,809
Operating loss	(47,014,645)	(22,330,809)
Nonoperating Revenues		
Grant revenue	47,014,645	22,329,906
Interest income (program income)	-	903
Change in net position	-	-
Net position, beginning	-	-
Net position, ending	\$ -	\$ -

The accompanying notes are an integral part of the financial statements.

New Mexico Health Insurance Exchange
Statements of Cash Flows
For the Year Ended December 31, 2014 and
for the Period Ended December 31, 2013

	2014	2013
Cash flows from operating activities		
Cash payments to employees for service	\$ (1,666,009)	\$ (657,092)
Cash payments to other suppliers of goods and services	<u>(33,017,541)</u>	<u>(18,188,169)</u>
Net cash used in operating activities	<u>(34,683,550)</u>	<u>(18,845,261)</u>
Cash flows from noncapital financing activities		
Grants received	34,899,999	19,860,801
Interest income received	<u>-</u>	<u>903</u>
Net cash provided by noncapital financing activities	<u>34,899,999</u>	<u>19,861,704</u>
Cash flows from capital and related financing activities		
Purchase of capital assets	<u>(25,140)</u>	<u>(141,574)</u>
Net cash used in capital and related financing activities	<u>(25,140)</u>	<u>(141,574)</u>
Net increase in cash	191,309	874,869
Cash, beginning of year	<u>874,869</u>	<u>-</u>
Cash, end of year	<u>\$ 1,066,178</u>	<u>\$ 874,869</u>
Reconciliation of operating loss to net cash used in operating activities		
Operating loss	\$ (47,014,645)	\$ (22,330,809)
Adjustments to reconcile operating loss to net cash used in operating activities		
Depreciation	51,670	7,582
Changes in operating assets and liabilities		
Premiums due	(39,968)	-
Due from New Mexico Health Insurance Alliance	26,849	(26,849)
Other receivables	1,832	(1,832)
Prepaid expenses and other assets	(4,072)	(17,499)
Account payable	10,271,515	3,388,623
Due to carriers	155,393	1,074
Due to New Mexico Health Insurance Alliance	(65,318)	62,495
Contract holdback	1,932,777	65,318
Accrued payroll and related expenses	13,384	6,636
Compensated absences	<u>(12,967)</u>	<u>-</u>
Net cash used in operating activities	<u>\$ (34,683,550)</u>	<u>\$ (18,845,261)</u>

The accompanying notes are an integral part of the financial statements.

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

1) Organization and Operations

Organization

The New Mexico Health Insurance Exchange (the “Exchange”) is a governmental entity organized pursuant to the New Mexico Health Insurance Exchange Act (the “Act”), New Mexico Statutes Annotated 1978, 59A-23F-1 through 23F-8. The Exchange was authorized by the New Mexico Legislature (the “Legislature”) in 2013 and began operations shortly thereafter on April 28, 2013; therefore, the 2013 period of operations was from April 28, 2013 through December 31, 2013 (the “period”). The Act replaces the New Mexico Health Insurance Alliance (the “Alliance”) that was created by the State of New Mexico in 1994. The purpose of the Exchange is to provide qualified individuals and qualified employers with increased access to health insurance.

The Act provides that the Exchange is a governmental entity for purposes of the Tort Claims Act (New Mexico Statutes Annotated [1978] 41-4-1 to 41-4-27), but neither the Board of Directors nor the Exchange shall be considered a governmental entity for any other purpose. However, given that the Exchange Board consists of members that are appointed pursuant to the Act, they meet the criteria for being considered a governmental entity; therefore, the Exchange must apply the accounting and financial reporting standards set by the Governmental Accounting Standards Board (GASB).

Patient Protection and Affordable Care Act (ACA) and Grant Proceeds

On March 23, 2010, the federal government passed the Patient Protection and Affordable Care Act (ACA). The ACA provides for guaranteed coverage to children up to age 19 and allowance for children up to age 26 to remain on their parent’s insurance. In addition, insurance carriers will be prohibited from making rescissions on any insured member. Beginning January 1, 2014, guaranteed issue was expanded to the 25-64 population.

In July 2010, the State of New Mexico, through its Office of Health Care Reform, filed for and received an initial \$1,000,000 Exchange Planning Grant. In September 2011, a second planning grant application for \$34,300,000 was filed and approved. In that grant application, the Alliance was named as the organization to house the insurance exchange for the State of New Mexico. On December 3, 2012, a Memorandum of Understanding was signed between the New Mexico Human Services Department and the Alliance whereby the Alliance was authorized to proceed with the establishment of an insurance exchange under provisions of the PPACA. On December 31, 2012, \$1,600,000 in grant funds were transferred to the Alliance and was presented as pass-through grant proceeds in the Alliance’s 2012 statement of financial position.

During the 2013 State of New Mexico legislative session, the Exchange legislation passed (Laws of 2013, Chapter 54). Under the new law, the Alliance Board ceased to exist and the Exchange Board supersedes the Alliance Board as the governing body. Once the Exchange was formed, the grant funds held by the Alliance were transferred to

New Mexico Health Insurance Exchange

Notes to the Financial Statements

December 31, 2014 and 2013

the Exchange's bank account for operating use. Effective January 1, 2015, the Alliance statutes (Laws 1994, Chapter 75, Sections 1 through 25) are repealed. A Memorandum of Understanding was executed in June 2014 between the Alliance and the Exchange to further define transition costs and final wind down responsibilities, which are expected to occur sometime in 2015.

Operations

The Exchange was established to provide access to quality health care for those without insurance, individuals that cannot afford health insurance offered at their place of employment, small businesses with 50 employees or fewer, and those that purchase their own insurance but would like more options.

All health insurance carriers and health maintenance organizations authorized to conduct business in New Mexico, and that meet the requirements of the rules promulgated in the Act, are eligible to participate in the Exchange. The Exchange performs its functions under the plan of operation established and approved pursuant to the Act and exercises its powers through the Board.

The Small Business Health Options Program (SHOP) was established as a program that allows small businesses, including nonprofits with up to 50 employees, to access health insurance through the Exchange. The SHOP functions as a conduit for insurance premiums as opposed to being either an insurer or reinsurer. All SHOP premiums billed and collected are recorded in the Exchange statement of net position with no activity impacting the statement of revenues, expenses and changes in net position. The Exchange does not withhold any portion of the SHOP premiums to cover administrative costs.

In November 2013, open enrollment began for 2014 for the SHOP. During the first open enrollment period, the Exchange used the Federal healthcare.gov technology for individual consumers, while design and development of the New Mexico based individual exchange was initiated, with implementation scheduled for the start of the second open enrollment period in October 2014.

In July 2014, the Exchange Board of Directors voted to continue using the Federal healthcare.gov technology solution for another year, to provide adequate time for testing the system. In October 2014 as the Exchange was finalizing its 2015 budget, which would also support a final grant request for system enhancements, the U.S. Centers for Medicare and Medicaid Services (CMS) notified the Exchange that they were not approving the eligibility verification model demonstrated to CMS during the Exchange's June 2014 Detail Design Review. CMS asked the Exchange to come into compliance with their single door eligibility verification model. Working with the technology vendor and Human Services Department (HSD), the Exchange developed cost estimates for complying with CMS's single door design. This estimate was added to the 2015 budget and the final budget was approved by the Exchange Board. The Board also authorized the

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

Exchange to request a final (Level 2) grant to fund the new development, which included the cost of system enhancements as well as the cost of coming into compliance with CMS's single door design mandate. The Level 2 grant, supported by the Board approved budget, was requested by the Exchange on November 14, 2014, and denied by CMS on December 18, 2014. The Exchange also requested a No Cost Extension (NCE) of its 3rd Level 1 grant in November 2014, and CMS approved the NCE on December 18, 2014.

Between December 2014 and March of 2015, the Exchange Board conducted a thorough cost-benefit analysis to determine what enrollment mechanism for the individual Exchange would best benefit New Mexicans and support the Exchange's goal of keeping operational costs low over time. Following this analysis, the Board decided that leasing the enrollment technology for the individual exchange from healthcare.gov, while continuing to run all other functions of the New Mexico State-Based Exchange, best supports the Exchange's mission of expanding access to high-quality and affordable health insurance. Additionally, based on the information available to the Exchange in March 2015, the option to lease federal technology is projected to cost less over a five year period of time than if New Mexico was to build its own technology solution. However, the option the Board selected carries some risk in that CMS has not yet defined the exact cost of a lease arrangement and the projected costs are estimates. Further, it is unknown if CMS will allow New Mexico to pay for the lease of technology from funds generated from New Mexico's market-wide carrier assessment or if the funds would need to come from another source. This uncertainty regarding the exact costs and payment structure represents a low to medium level of risk. CMS has indicated that these unknowns will likely be addressed through the official rule-making process later in 2015 and 2016.

The Exchange was required by the ACA to be financially sustainable by January 1, 2015, at which time, all costs associated with maintenance and operations of implemented systems, as well as routine operating costs related to those systems, such as rent and salaries expense, were no longer allowed to be funded by 1311 grant funds. During 2014, the Exchange Finance Committee evaluated various financial sustainability models and recommended to the Exchange Board a market-wide assessment of all major medical and Medicaid carriers, as allowed by the Act. After presenting the recommended financial sustainability model in two open committee meetings and two Board meetings, as well as providing a 30-day public comment period and a public hearing, the Exchange Board approved the financial sustainability plan on December 19, 2014.

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

2) Summary of Significant Accounting Policies

Accounting Principles

The financial statements of the Exchange have been prepared in accordance with accounting principles generally accepted in the United States of America as applied to governmental units and funds. The GASB is the standard-setting body for governmental accounting and financial reporting.

Basis of Presentation

The financial statements of the Exchange have been prepared using the economic resources measurement focus and the accrual basis of accounting. All of the Exchange's activities are reported as an enterprise fund.

The Exchange distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund's principal ongoing operations. Because the Exchange's operations were financed solely by federal grants in 2014 and 2013, there were no operating revenues reported. Operating expenses include the cost of providing services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses, which consists of grant revenue and interest income.

Revenues from grants that are restricted for specific uses are recognized as revenues and as receivables when the related costs are incurred. When both restricted and unrestricted resources are available, it is the Exchange's policy to use restricted resources first. Expenses are recorded when they are incurred. Expenses charged to federal programs are recorded utilizing the cost principles prescribed or permitted by the various funding sources.

Cash

For purposes of the statements of cash flows under proprietary fund accounting, the Exchange considers all unrestricted highly liquid investments with an initial maturity of three months or less to be cash equivalents. The Exchange did not have any cash equivalents as of December 31, 2014 or 2013.

Due from U.S. Department of Health and Human Services and Unearned Revenue

Various reimbursement procedures are used for awards received by the Exchange. Consequently, timing differences between expenditures and program reimbursements can exist at any time during the fiscal year. Amounts due from the U.S. Department of Health and Human Services at fiscal year-end represent an excess of accrual basis expenses over cash reimbursements received to date. Conversely, unearned revenue represents an excess of cash received (advance) over accrual basis expenses. Generally, these balances are

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

caused by differences in the timing of cash reimbursements and expenses and will be reversed in the remaining grant period.

Premiums Due

Premiums due consist of payments due from insured groups arising from the normal course of operations. The Exchange does not record an allowance against receivables from insured groups. Receivables from insured groups represent gross premium amounts receivable for insurance provided for which the payment is delinquent. These amounts are recovered by the Exchange either through subsequent collection or, if not collected, by cancellation of insurance coverage effective on the date through which premiums were paid.

Due to/ from New Mexico Health Insurance Alliance

Certain expenses, including wages and benefits of Alliance personnel, are shared between the Alliance and the Exchange based on an allocated percentage. During 2014, as a result of these transactions, shared service expenses totaled \$232,691 with no balances due to/due from the Alliance. During 2013, shared service expenses totaled \$49,573 and resulted in balances of \$65,318 due to the Alliance and \$26,849 due from the Alliance. The receivable and payable are presented on the statements of net position as Due to the Alliance and Due from the Alliance, and related expenses are recorded as salaries and benefits in the statements of revenues, expenses, and changes in net position.

Prepaid Expenses and Other Assets

Certain payments to vendors represent costs applicable to future accounting periods and are recorded as prepaid expenses and other assets in the statements of net position and expensed as the items are used.

Capital Assets and Depreciation

Capital assets are recorded at historical cost. Typically, personal property and equipment costing \$1,000 or more are capitalized in accordance with internal policy, in addition to outlays for items that significantly extend the useful life of a capital asset. This, however, does not preclude the Exchange from capitalizing costs below this amount when control over such assets is desired. Donated assets are recorded at their estimated fair value at the date of donation. Costs incurred for repair and maintenance are expensed as incurred.

Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. The estimated useful lives used to depreciate assets, by asset class, are as follows:

Furniture and fixtures	3 years
Equipment	3 years
Computer equipment and software	3 years

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

Due to Carriers

Due to carriers consists of payments made by insured groups during the normal course of operations that are owed to each insured groups respective insurance carriers. As a result of timing differences arising in the premium billing cycle, such amounts have been paid to the Exchange by insured groups, but not remitted by the Exchange to the respective insurance carriers at year-end.

Contract Holdback

In accordance with contractually agreed-upon terms with certain vendors, varying percentages of fees associated with contract deliverables are deliberately withheld by the Exchange until such deliverables have been completed. Those contract amounts that had accumulated, but had not been paid out to the various contractors at year-end, are recorded as a contract holdback liability on the statements of net position and are not included in accounts payable.

Compensated Absences

Under terms of employment, employees are granted sick leave and vacation in varying amounts. Full-time Exchange employees accumulate paid time off (PTO) hours for subsequent use according to the length of employment and within established maximum accrual limits. PTO may be accrued up to a maximum of two times an employee's annualized equivalent based on length of service. Hours in excess of the maximum personal leave available are written off and are not payable to the employee.

When employees terminate, they are compensated at their current hourly rate for accumulated unpaid PTO. All accumulated PTO is recorded as an expense and a liability in the Exchange's financial statements.

Net Position

The Exchange follows GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. Accordingly, the difference between assets, deferred outflows of resources, liabilities, and deferred inflows of resources, is referred to as net position. Net position is categorized as follows:

- ♦ *Net investment in capital assets*—Is intended to reflect the portion of net position which is associated with capital assets less outstanding capital asset related debt, if any. The Exchange has no capital asset related debt at December 31, 2014 or 2013.
- ♦ *Restricted net position*—Restricted net position results when constraints placed on an assets' use are either externally imposed by creditors, grantors, and contributions, or imposed by law through constitutional provisions or enabling legislation.
- ♦ *Unrestricted net position*—Represents net position not otherwise classified as invested in capital assets or restricted net position.

New Mexico Health Insurance Exchange

Notes to the Financial Statements

December 31, 2014 and 2013

Technology and Project Management

These expenses align with the “eligibility and enrollment” blueprint for building the Exchange. It includes expenditures incurred for the design, development and implementation of the Exchange eligibility and enrollment system. It also includes expenses related to project management, independent verification and validation, and expenses for changes to the State Medicaid eligibility verification system.

Consumer and Stakeholder Engagement and Support

These expenses align with the “Consumer and Stakeholder Engagement and Support” blueprint. It includes all marketing, advertising, media, public relations, stakeholder communications, enrollment entities, outreach entities, website development and referral call center vendors. All of these expenses are intended to educate consumers about the benefits of insurance. Marketing and advertising costs are expensed as incurred.

Operations

Operations expense includes all costs associated with running the Exchange, outside of salaries and benefits, such as recruitment, equipment, rent, telephone, insurance, equipment leases and supplies, outside of salaries and benefits.

Professional Services and Board

This includes all non-program contractual services, such as legal and audit expenses, as well as expenses related to monthly board meetings.

Plan Management

The Plan Management expense category aligns with the “Plan Management” blueprint and includes payments made to the Office of the Superintendent of Insurance for performance of Plan Management functions of the Exchange.

Income Taxes

The Exchange is a tax-exempt, quasi-governmental organization. Accordingly, no provision for income taxes has been included in the accompanying financial statements.

Use of Estimates

Financial statements prepared in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Fair Value of Financial Instruments

Financial instruments include various cash equivalents, receivables and payables. The carrying amount of these financial instruments has been estimated by management to approximate fair value primarily due to their short maturity.

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

Reclassifications

Certain amounts reported for the period ended December 31, 2013, have been reclassified to conform to the 2014 financial statement presentation. The reclassifications had no effect on the changes in net position for the period ended December 31, 2013.

Subsequent Events

Subsequent events through August 28, 2015, the date which the financial statements were available to be issued, were evaluated for recognition and disclosure in the December 31, 2014, financial statements.

In June 2015, in compliance with the financial sustainability plan, the Exchange issued its first carrier assessment for approximately \$4.7 million.

3) Custodial Credit Risk—Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Exchange's deposits may not be returned to it. The Exchange does not have a custodial credit risk policy requiring collateral on all deposits exceeding Federal Deposit Insurance Corporation (FDIC) limits, but the Exchange does have collateral that exceeds their total uninsured deposits. Bank deposits are insured by the FDIC up to \$250,000 per depositor per institution for interest-bearing and noninterest-bearing deposits. At times, portions of the cash balances in the financial institutions may exceed the insured limits. The Exchange has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash or cash equivalents.

At December 31, 2014 and 2013, the Exchange had deposits of \$1,250,097 and \$1,593,077, respectively. Of these total bank balances, there were no amounts subject to custodial credit risk as all amounts were either insured or collateralized as presented below.

	First National Bank of Santa Fe	
	2014	2013
Total amount on deposit	\$ 1,250,097	\$ 1,593,077
Less: FDIC insurance coverage	250,000	250,000
Total uninsured deposits	1,000,097	1,343,077
Pledged collateral, fair value	2,463,277	2,015,943
Pledged in excess	\$ (1,463,180)	\$ (672,866)

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

4) Capital Assets

A summary of capital assets activity is as follows:

	Balance at January 1, 2014	Increases	Decreases	Balance at December 31, 2014
Depreciable assets				
Furniture and fixtures	\$ 47,800	\$ 5,099	\$ -	\$ 52,899
Equipment	36,134	1,614	-	37,748
Computer software	32,787	1,868	-	34,655
Computer equipment	<u>24,853</u>	<u>16,559</u>	<u>-</u>	<u>41,412</u>
	<u>141,574</u>	<u>25,140</u>	<u>-</u>	<u>166,714</u>
Accumulated depreciation				
Furniture and fixtures	(2,904)	(17,128)	-	(20,032)
Equipment	(2,166)	(12,712)	-	(14,878)
Computer software	(1,822)	(11,499)	-	(13,321)
Computer equipment	<u>(690)</u>	<u>(10,331)</u>	<u>-</u>	<u>(11,021)</u>
	<u>(7,582)</u>	<u>(51,670)</u>	<u>-</u>	<u>(59,252)</u>
Total capital assets, net	<u>\$ 133,992</u>	<u>\$ (26,530)</u>	<u>\$ -</u>	<u>\$ 107,462</u>
	Balance at April 28, 2013 (inception)	Increases	Decreases	Balance at December 31, 2013
Depreciable assets				
Furniture and fixtures	\$ -	\$ 47,800	\$ -	\$ 47,800
Equipment	-	36,134	-	36,134
Computer software	-	32,787	-	32,787
Computer equipment	<u>-</u>	<u>24,853</u>	<u>-</u>	<u>24,853</u>
	<u>-</u>	<u>141,574</u>	<u>-</u>	<u>141,574</u>
Accumulated depreciation				
Furniture and fixtures	-	(2,904)	-	(2,904)
Equipment	-	(2,166)	-	(2,166)
Computer software	-	(1,822)	-	(1,822)
Computer equipment	<u>-</u>	<u>(690)</u>	<u>-</u>	<u>(690)</u>
	<u>-</u>	<u>(7,582)</u>	<u>-</u>	<u>(7,582)</u>
Total capital assets, net	<u>\$ -</u>	<u>\$ 133,992</u>	<u>\$ -</u>	<u>\$ 133,992</u>

Depreciation expense for the year ended December 31, 2014, was \$51,670 and for the period ended December 31, 2013, was \$7,582 and is reported in the statements of revenues, expenses, and changes in net position in operations expense.

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

5) Commitments

The Exchange is committed under various lease agreements for office space and office equipment which expire at varying times through December 31, 2017. These leases are classified as operating leases. Lease expenses for the year ended December 31, 2014, and for the period ended December 31, 2013, were \$91,339 and \$26,288, respectively. Lease expenses are included in operations expense in the accompanying statements of revenues, expenses, and changes in net position.

The following schedule details the future minimum lease payments as of December 31, 2014, for operating leases with initial or remaining lease terms in excess of one year:

Year ending December 31,		
2015		\$ 92,614
2016		68,440
2017		<u>4,184</u>
Total		<u>\$ 165,238</u>

Additionally, the Exchange has numerous professional and consulting service contracts and agreements for marketing and technology services in place with outstanding commitments at December 31, 2014 and 2013, of \$38.1 million and \$31.4 million, respectively. Such amounts are expected to be paid in 2015 through 2017.

6) Accrued Compensated Absences

A schedule of changes in the Exchange's accrued compensated absences is as follows:

Balance at January 1, 2014	Additions	Reductions	Balance at December 31, 2014	Amounts Due Within One Year
<u>\$ 62,495</u>	<u>\$ 50,696</u>	<u>\$ 63,663</u>	<u>\$ 49,528</u>	<u>\$ 49,528</u>

Balance at April 28, 2013	Additions	Reductions	Balance at December 31, 2013	Amounts Due Within One Year
<u>\$ -</u>	<u>\$ 63,168</u>	<u>\$ 673</u>	<u>\$ 62,495</u>	<u>\$ 62,495</u>

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

7) Retirement Plan

Beginning in 2014, the Exchange began sponsoring a 401(k) Retirement Plan (the “Plan”) to provide retirement benefits to its employees. The Plan allows eligible employees to defer a portion of their annual compensation pursuant to Section 401(k) of the Internal Revenue Code.

Under the terms of the Plan, all employees over the age of 18 may participate in the Plan after having fulfilled a one-month eligibility period in order to make contributions to the Plan. Employees are automatically enrolled into the Plan upon eligibility criteria having been fulfilled.

The Exchange matches 100% of an employee’s contributions up to 3% of total compensation and 50% of contributions that exceed 3% of compensation but that do not exceed 5% of compensation. The Exchange’s matching contributions to the Plan totaled \$29,777 for the year ended December 31, 2014.

In addition, all employees over the age of 18 may participate in receiving discretionary profit sharing contributions under the Plan after having fulfilled a 12-month eligibility period or having fulfilled 1,000 hours of service. Profit sharing contributions will be allocated to each eligible participant after the end of the Plan year. Any discretionary profit sharing contributions are determined by the Board; however, no such contributions were made to the Plan in 2014.

In 2013, the Exchange sponsored a Savings Incentive Match Plan for Employees (SIMPLE) IRA Plan. All employees were eligible to participate after having fulfilled a one-year eligibility period and received a minimum of \$5,000 in compensation as defined under the terms of the plan document. The Exchange made matching contributions limited to 3% of the participant’s compensation. For the period ended December 31, 2013, the Exchange contributed \$2,775 to the Plan.

8) Contingencies

Grants

Grant awards from federal governmental entities are subject to audits. Such audits could result in claims against the Exchange for disallowed costs or noncompliance with grantor restrictions. The amount, if any, of expenditures that may be disallowed by grantors cannot be determined at this time; although, the Exchange expects such amounts, if any, to be immaterial.

New Mexico Health Insurance Exchange
Notes to the Financial Statements
December 31, 2014 and 2013

Litigation

The Exchange is party to various legal proceedings that occur in the normal course of operations. Management does not believe that the outcome of these legal proceedings will have a material adverse impact on the Exchange. The Exchange maintains insurance coverage to protect against losses related to personal property and general liabilities, directors and officers, errors and omissions, and workers compensation.

Claims may also be filed for incidents that have occurred, including some of which the Exchange is not presently aware. Management believes that the amount of such potential claims, if any, would be immaterial to the Exchange. Accordingly, no accrual has been made for these potential claims.

9) New and Recently Issued Accounting Pronouncements

Recently Issued Accounting Pronouncements

The following GASB pronouncements have been issued, but are not effective at December 31, 2014:

- ◆ GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*
- ◆ GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*
- ◆ GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*

The Exchange will implement new GASB pronouncements, if applicable, no later than the required effective dates of each pronouncement. The Exchange believes that the above listed GASB pronouncements will not have any impact on the Exchange.

10) Economic Dependency

For 2014 and 2013, the Exchange received all of its revenues from grants funded by the United States Government.

Schedule of Expenditures of Federal Awards

New Mexico Health Insurance Exchange
Schedule of Expenditures of Federal Awards
December 31, 2014

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Pass-Through Grantor Number or Other Identifying Numbers	CFDA Number	Federal Expenditures
U.S. Department of Health and Human Services			
Cooperative agreement to support establishment of a state-operated health insurance exchange	N/A	93.525	\$ 47,014,645
Total U.S. Department of Health and Human Services			<u>\$ 47,014,645</u>

New Mexico Health Insurance Exchange
Notes to the Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2014

1) General

The accompanying schedule of expenditures of federal awards presents the federal award programs of the New Mexico Health Insurance Exchange (the “Exchange”). The Exchange’s reporting entity is defined in Note 1 to the basic financial statements. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

2) Basis of Accounting

The accompanying schedule of expenditures of federal awards is presented using the accrual basis of accounting, which is described in Note 1 to the basic financial statements. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

3) Catalog of Federal Domestic Assistance Award Numbers

Federal granting agencies are responsible for providing the Exchange with the Catalog of Federal Domestic Assistance (CFDA) number for each grant or contract.

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
New Mexico Health Insurance 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 the New Mexico Health Insurance Exchange (the "Exchange"), as of and for the year then ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the Exchange's basic financial statements and have issued our report thereon dated August 28, 2015.

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. Therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a deficiency in internal control, described in the accompanying schedule of findings and questioned costs as item 2014-001, that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Exchange's financial statements are free of 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*.

The Exchange's Response to Findings

The Exchange's response to the 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 the financial statements and, accordingly, we express no opinion on it.

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 Exchange'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 entities internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

REDW LLC

Albuquerque, New Mexico
August 28, 2015

Independent Auditor's Report on Compliance
With Requirements That Could Have a Direct and Material
Effect on Each Major Program and on Internal Control Over
Compliance in Accordance With OMB Circular A-133

Board of Directors
New Mexico Health Insurance Exchange

Report on Compliance for Each Major Federal Program

We have audited the New Mexico Health Insurance Exchange's (the "Exchange") compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the Exchange's major federal program for the year ended December 31, 2014. 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 the requirements of laws, regulations, contracts, and grants 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 OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 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 the major federal program. However, our audit does not provide a legal determination of the Exchange's compliance.

Opinion on the 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 its major federal program for the year ended December 31, 2014.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2014-002, 2014-003, and 2014-004. Our opinion on the major federal program is not modified with respect to these matters.

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

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 its major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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.

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.

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. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2014-002, 2014-003, and 2014-004 to be significant deficiencies.

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

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 OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

REDW LLC

Albuquerque, New Mexico
August 28, 2015

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs
For the Year Ended December 31, 2014

Section I — Summary of Auditor’s Results

Financial Statements

Type of auditor’s report issued:	Unmodified
Internal control over financial reporting: Material weaknesses identified?	No
Significant deficiencies reported?	Yes
Noncompliance material to financial statements noted?	No

Federal Awards

Type of auditor’s report issued on compliance for major programs:	Unmodified
Internal control over major programs: Material weaknesses identified?	No
Significant deficiencies reported?	Yes
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?	Yes

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section I — Summary of Auditor’s Results — continued

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
93.525	State Planning and Establishment Grants for Affordable Care Act (ACA) Exchanges

Dollar threshold used to distinguish
between type A and type B programs: \$1,410,439

Auditee qualified as low-risk auditee? No

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section II — Financial Statement Findings

2014-001 Financial Statement Segregation of Duties – Cash Disbursements (repeated and modified)

Condition: The Chief Financial Officer does not typically perform, but had access to perform for a portion of 2014, the following functions within the Exchange’s cash disbursements function:

- **Cash Disbursements:** Setup of new vendors and modification of existing vendors; entry of invoices into the accounting system; access to blank check stock, and printing, signing, and mailing of checks.
- **Payroll Disbursements:** Setup of new employees and modification or termination of existing employees; review of employee time sheets; entry of time sheets into the accounting system; access to blank payroll checks, and printing, signing, and distribution of payroll checks.

Criteria: Adequate segregation of duties should exist to mitigate the likelihood of errors or fraud in the accounts payable and payroll processes.

Cause: Adequate segregation of duties within the accounts payable and payroll processes has not been established.

Effect: When one employee can add vendors or employees and has access to signed checks, that employee may be able to disburse funds to fictitious or inappropriate vendors or employees without timely detection.

Auditor’s Recommendation: For practical reasons and costs considerations, the Exchange has a limited number of personnel to facilitate segregation of duties. However, duties between existing personnel should be allocated in such a manner to provide more robust segregation of incompatible duties. In 2014, an additional accountant was hired and the ADP Run system was implemented for payroll resulting in many of the segregation of duties issues identified above being resolved or mitigated. Management should continuously evaluate the cash disbursements cycle to determine if adequate controls exist and duties are properly segregated. Consider these key controls when making these assessments:

- **Cash Disbursements:** The responsibility for setting up new vendors and making changes to existing vendors should always be assigned and restricted to an individual independent of the cash disbursement process. An individual outside of the check preparation process should always review prepared checks and compare them to underlying support including invoices and be responsible for mailing the checks after they are signed.
- **Payroll Disbursements:** The responsibility for setting up new employees and making changes to existing employees should always be assigned and restricted to an individual independent of the payroll disbursement process. A thorough payroll register review should be conducted by someone outside of the payroll process to identify any unusual changes, hours, or pay rates.

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section II — Financial Statement Findings — continued

2014-001 Financial Statement Segregation of Duties – Cash Disbursements (repeated and modified) — continued

Management's Response: Management took all necessary corrective actions to resolve this finding in 2014 including:

1. The CFO is now restricted from processing accounts payable, entering journal entries and cash disbursements.
2. A comprehensive segregation of duties matrix was developed in October 2014, to thoroughly evaluate assignment of accounting activities to ensure that duties are segregated appropriately. Access rules were also evaluated in the accounting system, and all accounting policies and procedures were updated accordingly.
3. Vendor file maintenance and updating is now segregated to the Senior Accountant, who was hired in September 2014.
4. Payroll was outsourced to Automatic Data Processing (ADP) in June 2014, and responsibility for setting up new employees and making changes to existing employee payroll records was assigned and restricted to the Human Resources Manager.

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section III — Federal Award Findings and Questioned Costs

2014-002 — Allowable Costs (repeated and modified)

Federal program` information:

Funding agency:	U.S. Department of Health and Human Services
Title:	State Planning and Establishment Grants for ACA Exchanges
CFDA number:	93.525
Award number:	HBEIE140187, HBEIE140185, HBEIE140193, HBEIE130170

Criteria: According to OMB Circular A-87, to be allowable under Federal awards, costs must be necessary and reasonable for proper and efficient performance and administration of Federal awards, authorized or not prohibited under State or local laws or regulations, and adequately documented. In addition, the U.S. Department of Health and Human Services (HHS) internal policy, “HHS Policy on Promoting Efficient Spending” Attachment Three, prohibits using any appropriated funds to purchase promotional items that are not a necessary expense that directly furthers the organization’s mission.

Condition: The Exchange purchased various promotional items as part of a marketing campaign. Upon analysis of vendor invoices and the items purchased, we identified several instances where promotional items lacking informational value were purchased and paid for by the Exchange utilizing federal funds.

Questioned Costs: \$4,844

Context: Four of 23 disbursements charged to “marketing expenses” in 2014 were for items that were promotional in nature and did not appear to directly further the Exchange’s mission.

Cause: Exchange personnel were unaware that promotional items were specifically restricted; therefore, certain marketing materials were purchased with only the Exchange’s logo rather than additional information (i.e. mission, purpose, guidance, etc.) that would qualify the materials as “informational” rather than “promotional” in nature.

Effect: The Exchange is not in compliance with OMB Circular A-87 and HHS’s policy and used federal funds on unallowable costs.

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section III — Federal Award Findings and Questioned Costs — continued

2014-002 — Allowable Costs (repeated and modified) — continued

Auditor's Recommendations: Exchange personnel should further research the types of expenses that are allowed and not allowed under OMB Circular A-87 and HHS policies. All vendor invoices and purchasing decisions should be reviewed to ensure that the expenses are allowable. If goods or services are needed and they are not allowable, other Exchange income, if available, should be used to pay for those expenses, or they should not be purchased. Furthermore, the Exchange should establish a formal policy for distinguishing between “promotional” and “informational” items, including documenting why certain purchases meet the definition of “informational” and further the Exchange’s mission.

Management's Response: Management thought it was in compliance with OMB Circular A-87, in writing to the State Officer and seeking permission to use 1311 grant funds for promotional items. While permission was granted, the permission anticipated further research to fully understand that promotional materials were allowed only if they provided enough information to direct consumers to the Exchange. Management has modified its processes to ensure that all promotional materials provide the requisite information if paid for with 1311 grant funding. Furthermore, Management will ensure that all purchasing decisions and vendor invoices are thoroughly reviewed to ensure that expenses are allowable.

Beginning mid-2015, 1311 grant funding will no longer be available for marketing and outreach expenses unless incurred for the design, development, and implementation of systems, tools and processes.

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section III — Federal Award Findings and Questioned Costs — continued

2014-003— Procurement (repeated and modified)

Federal program information:

Funding agency:	U.S. Department of Health and Human Services
Title:	State Planning and Establishment Grants for ACA Exchanges
CFDA number:	93.525
Award number:	HBEIE140187, HBEIE140185, HBEIE140193, HBEIE130170

Criteria: According to 45 CFR part 92.36, grantees and subgrantees will use their own procurement procedures which reflect applicable state and local laws and regulations, provided that the procurements conform to applicable federal law and the standards identified in this section. Additionally, all procurement transactions will be conducted in a manner providing full and open competition, and will have written selection procedures.

Condition: The Exchange operated for the first three months of fiscal year 2014 without procurement policies and procedures in place. During this time, the Exchange entered into procurement transactions with certain vendors without written selection procedures. Additional policies and procedures were developed in March 2014 to guide the procurement process and Exchange personnel attended training on OMB Circulars A-87 and A-133. We did not identify any noncompliance with the procurement policies and procedures established after March 2014.

Questioned Cost: None.

Context: All procurement transactions in the first three months of the year.

Cause: The Exchange did not approve and begin implementing formal procurement policies and procedures until March 2014. In addition, prior to training received in mid-2014, Exchange personnel lacked experience operating federal grants and applicable OMB circulars, including Circulars A-87 and A-133.

Effect: The Exchange was not in compliance with federal procurement requirements for the first three months of 2014.

Auditor's Recommendations: Management should continue to enforce the new procurement policies and procedures and require regular training for both new and existing Exchange personnel on the evolving requirements of OMB circulars.

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section III — Federal Award Findings and Questioned Costs — continued

2014-003— Procurement (repeated and modified) — continued

Management's Response: Management took steps to correct this deficiency by implementing a procurement policy in March 2014 and developing related policies to cover all purchases, including those under \$100,000. The Exchange accounting staff attended training on OMB Circulars A-87 and A-133 in August 2014. Exchange leadership has also been trained on OMB Circulars A-87 and A-133. Training will be required for all newly hired accounting staff and leadership as part of the on-boarding process.

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section III — Federal Award Findings and Questioned Costs — continued

2014-004 — Suspension and Debarment (repeated and modified)

Federal program information:

Funding agency:	U.S. Department of Health and Human Services
Title:	State Planning and Establishment Grants for ACA Exchanges
CFDA number:	93.525
Award number:	HBEIE140187, HBEIE140185, HBEIE140193, HBEIE130170

Criteria: According to 45 CFR part 92.35, “grantees and subgrantees” must not make any award or permit any award (subgrant or contract) at any tier to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in federal assistance programs under Executive Order 12549, Debarment and Suspension.

Condition: Beginning in early 2014, a suspension and debarment clause was added to all Exchange contracts; however, this was not done for all contracts at the beginning of 2014. In addition, the Exchange operated through September 2014 without a policy or procedure in place to verify contractors are not suspended or debarred. Up until September 2014, there was no consistent process for checking suspension and debarment prior to entering into purchase agreements.

Questioned Cost: None.

Context: All vendors paid in excess of \$25,000.

Cause: The Exchange did not approve formal suspension and debarment policies and procedures until September 2014. In addition, prior to the training received in mid-2014, Exchange personnel lacked experience operating federal grants and applicable OMB circulars, including Circulars A-87 and A-133.

Effect: The Exchange was not in compliance with federal suspension and debarment requirements for a portion of 2014. The Exchange ran the risk of contracting with a vendor who is suspended or debarred.

Auditor’s Recommendations: Management should enforce the new suspension and debarment policies and procedures to ensure that the Exchange is performing their due diligence prior to entering into purchasing agreements with potential vendors. While self-attestation through the vendor contracts is helpful, it only partially mitigates the risk of the Exchange entering into an agreement with a vendor that is suspended or debarred. Exchange personnel should continue to receive regular training on OMB Circulars A-87 and A-133, as well as the new Uniform Guidance referred to as the “Super Circular”

New Mexico Health Insurance Exchange
Schedule of Findings and Questioned Costs — continued
For the Year Ended December 31, 2014

Section III — Federal Award Findings and Questioned Costs — continued

2014-004 — Suspension and Debarment (repeated and modified) — continued

Management's Response: Management corrected this deficiency in 2014 by incorporating the suspension and debarment verification process in the vendor evaluation process. Suspension and debarment verification has also been added to the accounts payable vendor setup process for all new vendors.

New Mexico Health Insurance Exchange
Summary Schedule of Prior Audit Findings
For the Year Ended December 31, 2014

Prior Audit Findings	Current Status
2013-001 Financial Statement Segregation of Duties – Cash Disbursements	Unresolved – Refer to finding 2014-001
2013-002 Financial Statement Adjustments	Resolved
2013-003 Allowable Costs	Unresolved – Refer to finding 2014-002
2013-004 Procurement	Unresolved – Refer to finding 2014-003
2013-005 Suspension and Debarment	Unresolved – Refer to finding 2014-004
2013-006 Supporting Documentation	Resolved

**New Mexico Health Insurance Exchange
Corrective Action Plan
For the Year Ended December 31, 2014**

Audit Finding	Corrective Action Plan	Person(s) Responsible	Estimated Completion Date
2014-002 – Allowable Costs	See management’s response in the schedule of findings and questioned costs	Chief Financial Officer	June 30, 2015
2014-003 – Procurement	See management’s response in the schedule of findings and questioned costs	Chief Financial Officer	August 31, 2015
2014-004 – Suspension and Debarment	See management’s response in the schedule of findings and questioned costs	Chief Financial Officer	June 30, 2015

New Mexico Health Insurance Exchange
Exit Conference
December 31, 2014

An exit conference was held on June 24, 2015, with the Exchange. The conference was held at the Exchange's offices in Albuquerque, New Mexico. In attendance were:

NM Health Insurance Exchange

Chief Executive Officer (CEO)

Chief Finance Officer (CFO)

REDW_{LLC}

Laurel Shelton, Principal

Halie Garcia, Senior Manager

In addition, a presentation was made to an open session of the Board of Directors on August 28, 2015.