

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**COLORADO DID NOT ALWAYS
COMPLY WITH FEDERAL
REQUIREMENTS WHEN EXPENDING
FEDERAL ESTABLISHMENT GRANT
FUNDS ALLOCATED FOR ITS SHARED
ELIGIBILITY SYSTEM COSTS**

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Office of Inspector General

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OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS

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Report in Brief

Date: April 2018

Report No. A-07-16-02804

U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES
OFFICE OF INSPECTOR GENERAL



Why OIG Did This Review

The Patient Protection and Affordable Care Act (ACA) established health insurance exchanges (“marketplaces”) to allow individuals and small businesses to shop for health insurance in all 50 States and the District of Columbia. The ACA provided grants to States for planning, establishing, and early operation of marketplaces. This review is part of a series of reviews of establishment grants for State marketplaces across the Nation, including several reviews of Connect for Health Colorado (Colorado marketplace).

Our objective was to determine whether the Colorado marketplace complied with Federal requirements when expending establishment grant funds allocated for its Shared Eligibility System (SES) costs.

How OIG Did This Review

We reviewed the \$183.7 million that the Centers for Medicare & Medicaid Services (CMS) awarded to the Colorado marketplace during Federal fiscal year (FY) 2012 through the third quarter of FY 2016. We focused on the allocation of SES costs to the Colorado marketplace by the Colorado Department of Health Care Policy and Financing (HCPF), the State Medicaid agency, for the development and implementation of the SES, which is an automated system modified from HCPF’s existing Medicaid eligibility system.

Colorado Did Not Always Comply With Federal Requirements When Expending Federal Establishment Grant Funds Allocated for Its Shared Eligibility System Costs

What OIG Found

The Colorado marketplace did not always comply with Federal requirements when expending Federal establishment grant funds allocated for its SES costs. Specifically, the Colorado marketplace allowed SES costs to be allocated to it on the basis of an arbitrary 50/50 cost allocation ratio, contrary to requirements and guidance that the methodology for allocation (1) be based on expected transactions and expected program population and (2) not be arbitrary. In addition, the Colorado marketplace allowed SES costs totaling \$2.1 million to be allocated to the incorrect cost allocation plan (CAP) period.

SES costs were not always properly allocated to the Colorado marketplace because it did not have written policies that explained how to develop a CAP and because it did not maintain documentation for the cost allocation ratio. In addition, the marketplace did not have adequate internal controls.

What OIG Recommends

We make procedural recommendations to the Colorado marketplace for the development and implementation of a cost allocation methodology and for the development and implementation of written policies, reinforced by adequate internal controls, that explain how to develop a CAP, how to provide formal input to HCPF and CMS during the development of cost allocation ratios, and how to adequately document the development of those ratios. We also recommend that the Colorado marketplace develop and implement written policies and procedures to ensure that future Federal grant award costs are allocated to it in accordance with Federal requirements.

The Colorado marketplace neither agreed nor disagreed with our recommendations but in its comments described corrective actions that it had implemented or planned to implement to address those recommendations. According to the Colorado marketplace, these corrective actions included developing a CAP that was approved by CMS in September 2017, developing processes to evaluate proposed allocation methodologies, and modifying accounting processes and procedures to more accurately track costs.

TABLE OF CONTENTS

| | |
|---|----|
| INTRODUCTION..... | 1 |
| Why We Did This Review | 1 |
| Objective | 1 |
| Background | 2 |
| Patient Protection and Affordable Care Act | 2 |
| Federal Requirements Related to Cost Allocation and Enhanced Funding for Marketplaces | 2 |
| Health Insurance Marketplace Programs | 3 |
| The Colorado Marketplace | 3 |
| Colorado’s Shared Eligibility System..... | 4 |
| Shared Eligibility System Cost Allocation..... | 4 |
| How We Conducted This Review | 5 |
| FINDINGS..... | 6 |
| The Colorado Marketplace Allowed Shared Eligibility System Costs To Be Allocated to It on the Basis of an Arbitrary Cost Allocation Plan..... | 6 |
| Federal Requirements..... | 7 |
| Lack of Support That Shared Eligibility System Costs Were Properly Allocated | 7 |
| Lack of Written Policies and Supporting Documentation and Lack of Oversight | 9 |
| The Colorado Marketplace Allowed Shared Eligibility System Costs To Be Allocated to the Incorrect Cost Allocation Plan Period | 9 |
| Federal Requirements..... | 10 |
| Shared Eligibility System Costs Incurred in the Initial Cost Allocation Period That Were Improperly Allocated to the Colorado Marketplace..... | 10 |
| Inadequate Internal Controls..... | 12 |
| RECOMMENDATIONS | 13 |
| AUDITEE COMMENTS | 13 |
| APPENDICES | |
| A: Audit Scope and Methodology | 14 |

| | |
|---|----|
| B: Federal Grants to States for Planning, Establishing, and Early Operation of Marketplaces | 16 |
| C: Federal Grants Awarded for Establishing and Early Operation of the Colorado Marketplace as of December 31, 2016 | 19 |
| D: Shared Eligibility System Costs Allocated to the Colorado Marketplace | 20 |
| E: Auditee Comments | 21 |

INTRODUCTION

WHY WE DID THIS REVIEW

The Patient Protection and Affordable Care Act (ACA)¹ established health insurance exchanges (commonly referred to as “marketplaces”) to allow individuals and small businesses to shop for health insurance in all 50 States and the District of Columbia. The ACA provided grants² to States for planning, establishing, and early operation of marketplaces.

Connect for Health Colorado (Colorado marketplace) is a quasi-governmental agency that administers the State’s establishment grants and is responsible for complying with applicable Federal grant requirements. The Colorado marketplace used the Shared Eligibility System (SES), an automated system developed and maintained by the State’s Medicaid agency, for eligibility determination and enrollment services.

This review is part of a series of reviews of establishment grants for State marketplaces across the Nation. We selected the individual State marketplaces to cover States in different parts of the country. We have conducted and are conducting additional audit work at the Colorado marketplace. See “Affordable Care Act Reviews” on the Office of Inspector General (OIG) website for a list of related OIG reports on marketplace operations.³

OBJECTIVE

Our objective was to determine whether the Colorado marketplace complied with Federal requirements when expending Federal establishment grant funds⁴ allocated for its SES costs.

¹ P.L. No. 111-148 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, P.L. No. 111-152 (Mar. 30, 2010), collectively referred to as “ACA.”

² Under section 1311(a) of the ACA, the Centers for Medicare & Medicaid Services (CMS) provided several different funding opportunities available to States, including Early Innovator Cooperative Agreements, Planning and Establishment Grants, and Establishment Cooperative Agreements. See Appendix B for more detailed information about the types of grants and cooperative agreements available to States related to the establishment of a marketplace.

³ Available online at <https://oig.hhs.gov/reports-and-publications/aca/>.

⁴ For purposes of this report, we reviewed Level One and Level Two grants. See Appendix B for more detailed information about Level One and Level Two grants.

BACKGROUND

Patient Protection and Affordable Care Act

Within the Department of Health and Human Services' (HHS) CMS, the Center for Consumer Information and Insurance Oversight (CCIIO)⁵ is responsible for implementing many of the requirements of the ACA, including overseeing the implementation of provisions related to the marketplaces and the private health insurance plans offered through the marketplaces. These plans are known as qualified health plans (QHPs).

A marketplace performs many functions, such as certifying QHPs; determining eligibility for premium tax credits and cost-sharing reductions; responding to consumer requests for assistance; and providing a website and written materials that individuals can use to assess their eligibility, evaluate health insurance coverage options, and enroll in selected QHPs (ACA § 1311(d)(4)). Additionally, a marketplace helps a State to coordinate eligibility for and enrollment in other State-based public health care programs, such as Medicaid and the Children's Health Insurance Program (CHIP).

Federal Requirements Related to Cost Allocation and Enhanced Funding for Marketplaces

CCIIO's Establishment Grant Funding Opportunity Announcements and the Colorado marketplace's Notice of Grant Awards (NGA) terms and conditions require the SES costs to be allocated among Medicaid, CHIP, and the Colorado marketplace consistent with cost allocation principles.⁶ CMS provides supplemental guidance to States that is specific to cost allocation for the marketplaces in *Guidance for Exchange and Medicaid Information Technology (IT) Systems* (version 2.0, May 2011) and *Supplemental Guidance on Cost Allocation for Exchange and Medicaid Information Technology (IT) Systems Questions and Answers* (October 5, 2012). Primarily, CMS supplemental guidance says: "States are expected to update their cost allocation methodology and plan based on updated or better data"⁷

⁵ To implement and oversee the ACA's marketplace and private health insurance requirements, HHS established the Office of Consumer Information and Insurance Oversight (OCIIO) in April 2010 as part of the HHS Office of the Secretary. In January 2011, OCIIO was transferred to CMS under a new center named CCIIO (76 Fed. Reg. 4703 (Jan. 26, 2011)). In this report, we use "CCIIO" to refer to both OCIIO and CCIIO.

⁶ Office of Management and Budget (OMB) Circular No. A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, was relocated to 2 CFR part 225 and made applicable by 45 CFR § 92.22(b). (HHS has promulgated new grant regulations and cost principles at 45 CFR part 75 that apply to awards made on or after Dec. 26, 2014.)

⁷ CMS issued further supplemental guidance, which states: "CMS strongly recommends that states continue to reassess their cost allocation on an annual basis and/or if there is a substantive change in program participation . . ." or whenever a State seeks additional funding (*FAQs on the Use of 1311 Funds, Project Periods, and updating the cost allocation methodology* (Sept. 2014)).

State Medicaid agencies must submit Implementation Advance Planning Documents (IAPDs) to obtain enhanced Federal funding⁸ for Medicaid information technology (IT) system projects related to Medicaid eligibility and enrollment, including eligibility and enrollment through a marketplace system (42 CFR § 433.112).

States must also establish Cost Allocation Plans (CAPs) that identify, measure, and allocate costs to each State-operated program (45 CFR part 95, subpart E). A State must promptly amend its CAP if there are significant changes in program levels or a material defect is discovered in its CAP (45 CFR §§ 95.509(a)(1) and (2)).

Health Insurance Marketplace Programs

The ACA provided for funding assistance⁹ to a State for the planning and establishment of a marketplace that incorporates eligibility determination and enrollment functions for all consumers of participating programs, such as Medicaid and private health insurance offered through a marketplace (ACA § 1311).

See Appendix B for details on the Federal assistance available to States to establish marketplaces.

The Colorado Marketplace¹⁰

The Colorado General Assembly passed legislation in May 2011 creating the Colorado marketplace (originally COHBE) as a “non-profit, unincorporated public entity” that is an “instrumentality of the state” but is not a State agency.¹¹ This legislation includes a provision for the appointment and duties of a Board of Directors (Board) of the marketplace.

The Colorado marketplace provides eligibility determination and enrollment services for QHPs using the SES, an automated system developed and maintained by the Colorado Department of Health Care Policy & Financing (HCPF), the agency that administers the Medicaid program in Colorado.

⁸ Enhanced funding refers to 90-percent and 75-percent Federal financial participation (FFP), which is greater than the 50-percent FFP available for most Medicaid administrative expenses.

⁹ Projects and programs are carried out under a variety of types of grants, including the use of a specific type of grant known as a cooperative agreement. When a Federal agency expects to be substantially involved in carrying out the project or program, it awards a cooperative agreement (*HHS Grants Policy Statement*, p. ii).

¹⁰ Documents relevant to and cited in this report use these terms interchangeably: Connect for Health Colorado, C4HCO, Colorado Health Benefit Exchange, the Colorado Health Benefit Exchange (COHBE), Colorado Exchange, and Colorado marketplace. For that reason, this report will from time to time use one of these other terms to refer to the Colorado marketplace.

¹¹ Colorado Senate Bill 11-200, signed Jun. 1, 2011.

Colorado's Shared Eligibility System

The SES is a system adapted and modified from HCPF's existing Medicaid eligibility system. In a December 2014 Memorandum of Understanding (MOU) between the two entities, the Colorado marketplace and HCPF agreed that it was in the public interest to find ways to operate efficiently and coordinate effectively by minimizing the duplication of services and leveraging limited resources. The SES thus supports the business functions of the Colorado marketplace, including application and enrollment, plan management, and consumer assistance; among other things, it determines whether enrollees qualify for Medicaid or a QHP. The SES was not operational for the Colorado marketplace's first open enrollment period (October 2013 to March 2014) but was for the second (November 2014 to February 2015) and third (November 2015 to January 2016) open enrollment periods. The Colorado marketplace received several Federal grants for planning, establishing, and early operation of the marketplace.

Shared Eligibility System Cost Allocation

In August 2012, HCPF submitted an IAPD (version 4) to CMS for review. IAPD version 4 stated that the Colorado marketplace and HCPF would fund the interoperability requirements between the State and marketplace systems to support a "no wrong door" eligibility experience.¹² An important provision of IAPD version 4 was that SES costs would be allocated between the Colorado marketplace and HCPF.

In turn, the CAP associated with IAPD version 4 identified those project costs that would be allocated between the two entities. This CAP also allocated those costs based on the estimated enrollments of those members of Colorado's population who were eligible for Medicaid through HCPF (one-third) and those who were eligible for QHPs through the Colorado marketplace (two-thirds). Colorado commissioned a study of projected marketplace enrollment and based the estimated enrollments cited in this CAP on the study's results.¹³

IAPD version 4 also stated that HCPF would submit a revised CAP based on actual enrollment statistics from the first year of the Colorado marketplace's operations. CMS approved IAPD version 4 on January 2, 2013. CMS's approval letter specified an initial allocation of costs as a ratio of two-thirds to the Colorado marketplace and one-third to HCPF—the same ratio as in

¹² The "no wrong door" concept means that an applicant can enroll in a health plan regardless of which online system (the State Medicaid system or the Colorado marketplace) that applicant uses as an entry point.

¹³ Gruber, J. (Jan. 2012). *Report on RFP COHIEX #0001: For an Independent Consulting Firm to Conduct Background Research to Support the Development of the Colorado Health Benefit Exchange*. At <http://connectforhealthco.com/COHBE/media/COHBE/PDFs/DAWG/Gruber-modeling-report-narrative-january-2012.docx> (accessed Aug. 31, 2017). This report is also mentioned in the IAPD on the Eligibility Determination System (version 5.1) that HCPF, in collaboration with the Governor's Office of Information Technology, the Colorado Department of Human Services, and Colorado Counties, submitted on Apr. 5, 2013, to CMS for approval.

the CAP associated with IAPD version 4. Although CMS approved the initial CAP, the approved cost allocation ratio associated with it was never used to allocate SES costs.

On May 15, 2014, HCPF submitted a revised IAPD (version 7) to CMS. This IAPD and its associated CAP retained many provisions of IAPD version 4, including the statement that SES costs would be allocated between the Colorado marketplace and HCPF. However, IAPD version 7 proposed a revision of the cost allocation percentages: 50 percent of costs would be allocated to HCPF and 50 percent to the Colorado marketplace. This revised IAPD stated that HCPF and the Colorado marketplace had negotiated the revised CAP to ensure the best use of Federal funds and the sustainability of the Colorado marketplace. CMS approved IAPD version 7, and its 50/50 cost allocation ratio, on September 30, 2014.

For this report, we refer to the time period between CMS's approval of IAPD version 4 (January 2, 2013) and CMS's approval of IAPD version 7 (September 30, 2014) as the "initial CAP period." We refer to the time period after CMS's approval of IAPD version 7 as the "revised CAP period." Our audit period ended on June 30, 2016. (See "How We Conducted This Review" below.)

As of December 31, 2014, CCIIO had awarded Colorado three establishment grants and a post-award amendment to the third of the three grants totaling \$183.7 million.

See Appendix C for details about grants awarded for establishing and early operation of the Colorado marketplace as of December 31, 2014.

HOW WE CONDUCTED THIS REVIEW

We reviewed the NGAs associated with the \$183.7 million that CCIIO awarded to the Colorado marketplace—three establishment grants and a post-award amendment to the third of the three grants—beginning February 22, 2012, through June 30, 2016. Because CMS permitted States to request No-Cost Extensions (NCEs) for the use of establishment grant funds after January 1, 2015, for activities not related to the operational costs of their marketplaces, and because the Colorado marketplace requested and received an NCE,¹⁴ we extended our audit period to June 30, 2016. We limited our review of internal controls to the systems and procedures for allocating and claiming costs to establishment grants and to Medicaid. We obtained an understanding of how the Colorado marketplace and HCPF developed the cost allocation methodologies.

We previously reported on the Colorado marketplace's expenditure of establishment grant funds (A-07-14-02801, Dec. 27, 2016). We are still conducting audit work on several aspects of the Colorado marketplace's operations and will report separately on its accounting system. We conducted this performance audit in accordance with generally accepted government

¹⁴ CMS, *FAQs on the Use of 1311 Funds and No-Cost Extensions* (Mar. 2014). CMS approved the Colorado marketplace's request for an NCE in November 2014.

auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix A contains the details of our audit scope and methodology.

FINDINGS

The Colorado marketplace did not always comply with Federal requirements when expending Federal establishment grant funds allocated for its SES costs. Specifically, the Colorado marketplace allowed:

- SES costs to be allocated to it on the basis of an arbitrary, 50/50 cost allocation ratio, contrary to Federal requirements and to CMS supplemental guidance that the methodology for allocation (1) be based on expected transactions and expected program population and (2) not be arbitrary; and
- SES costs totaling \$2,110,378 that were incurred, either entirely or in part, during the *initial* CAP period to be improperly allocated to it because the marketplace used the cost allocation ratio in effect for the *revised* CAP period.

SES costs were not always properly allocated to the Colorado marketplace because it did not have written policies that explained how to develop a CAP based on relative benefits received and because it did not maintain documentation for the cost allocation ratio. In addition, the marketplace did not have adequate internal controls to ensure that these costs were properly allocated to it by HCPF using the cost allocation ratios in effect for the appropriate CAP period.

THE COLORADO MARKETPLACE ALLOWED SHARED ELIGIBILITY SYSTEM COSTS TO BE ALLOCATED TO IT ON THE BASIS OF AN ARBITRARY COST ALLOCATION PLAN

The Colorado marketplace allowed SES costs to be allocated to it that were not based on the relative benefits received, contrary to the provisions of 2 CFR part 225. The marketplace did so because an unallowable methodology was used to allocate SES costs to its establishment grants for its health insurance marketplace. Specifically, the Colorado marketplace and HCPF used an arbitrary 50/50 cost allocation ratio but did not maintain any documentation showing that the methodology for allocation was based on expected transactions or expected enrollment.

Federal Requirements

For a cost to be allowable, it must be allocable to a Federal award (2 CFR part 225, Appendix A, § C.1). A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to that cost objective in accordance with the relative benefits received (2 CFR part 225, Appendix A, § C.3).

As stated earlier in “Federal Requirements Related to Cost Allocation and Enhanced Funding for Marketplaces,” CMS supplemental guidance requires that prospective adjustments be based on updated or better data. This guidance also states: “Consistent with the cost allocation principles outlined in OMB Circular A-87, the methodology for allocation should have some reasoning based on expected transactions, expected program population, etc., and cannot be arbitrary (e.g., simply half and half because there are two programs sharing in the investment)” (*Supplemental Guidance on Cost Allocation for Exchange and Medicaid Information Technology (IT) Systems Questions and Answers*, October 5, 2012).

Lack of Support That Shared Eligibility System Costs Were Properly Allocated

Initial and Revised Allocations of Shared Eligibility System Costs

The methodology for allocation conveyed in the initial CAP (IAPD version 4) was consistent with Federal requirements and CMS supplemental guidance. Specifically, the Colorado marketplace allowed SES costs to be allocated to it based on estimated enrollments of those members of Colorado’s population who were eligible for either Medicaid through HCPF or for QHPs through the Colorado marketplace. On the basis of those estimated enrollments and as conveyed in the CAP associated with IAPD version 4, the Colorado marketplace accepted the initial CAP, which allocated one-third of SES costs to HCPF and two-thirds of those costs to the marketplace. This cost allocation ratio remained in place until HCPF submitted IAPD version 7, which revised that ratio to a 50/50 basis. See Table 1 on the following page.

Table 1: Cost Allocation Plan Effective Dates

| CAP | Ratio | Effective Date |
|-------------|---|-------------------------------|
| Initial CAP | Two-thirds (approximately 67%) of the SES costs allocated to Colorado marketplace and one-third (approximately 33%) allocated to HCPF | January 2, 2013 ¹⁵ |
| Revised CAP | 50% of the SES costs allocated to Colorado marketplace and 50% allocated to HCPF (50/50 cost allocation ratio) | September 30, 2014 |

However, although IAPD version 7 conveyed the revised cost allocation ratio, neither the Colorado marketplace, nor HCPF, nor CMS could provide documentation supporting that the ratio was based on relative benefits received. Furthermore, the Colorado marketplace could not provide documentation supporting that the ratio was based on updated or better enrollment data—that is, that the ratio was based on expected transactions or expected program population. Accordingly, the revised cost allocation was based on an arbitrary 50/50 ratio that the Colorado marketplace had negotiated with HCPF. CMS approved IAPD version 7, which included the revised CAP, on September 30, 2014.

We have requested from the Colorado marketplace, HCPF, and CMS, documentation that was used to develop the revised cost allocation ratio; we did so to determine whether the 50/50 cost allocation ratio was based on an acceptable methodology. However, as of September 2017, none of these entities has provided any supporting documentation or has been able to explain the basis for this ratio to us, other than to say that it was a negotiated rate.

Revised Cost Allocation Ratio Not Supported by Updated, Better Data

The lack of documentation and absence of explanation heighten the risk that the Colorado marketplace allowed SES costs to be allocated to it that were not based on the relative benefits received by the program. Data that became available to both the Colorado marketplace and HCPF after the first enrollment period showed that enrollment numbers significantly deviated from the initial CAP’s allocation of one-third of the SES costs to HCPF and two-thirds of those costs to the Colorado marketplace. In fact, enrollment statistics for that first enrollment period

¹⁵ January 2, 2013, is the effective date of the initial CAP. Before that date, SES costs were accumulated but were neither assigned to the Colorado marketplace nor allocated. HCPF did not assign any SES costs to the marketplace until January 2015. At that point, costs were allocated based on the revised CAP, i.e., the 50/50 ratio.

were almost the opposite of what had been projected, with nearly two-thirds of the enrollment activity having been related to HCPF and one-third of that activity having been related to the Colorado marketplace.

In spite of this information, HCPF revised the CAP to allocate SES costs to HCPF and the Colorado marketplace based on an arbitrary 50/50 ratio that it had negotiated with the marketplace. By the time the SES became operational during the second enrollment period, HCPF had submitted the revised IAPD version 7 and its associated CAP which, except for a few cost line items, allocated costs on a 50/50 basis to HCPF and the Colorado marketplace. This cost allocation ratio was not supported by the updated, better data (that is, the enrollment statistics for the first enrollment period) that had become available. Nevertheless, the Colorado marketplace allowed this arbitrary 50/50 cost allocation ratio to be used to improperly allocate SES costs.

Lack of Written Policies and Supporting Documentation and Lack of Oversight

SES costs were not always properly allocated to the Colorado marketplace because it did not have written policies that explained how to develop a CAP based on relative benefits received. Specifically, the Colorado marketplace relied heavily on HCPF and was not actively involved in the ratio determination process. HCPF communicated with CMS through the IAPD version 7 about the 50/50 cost allocation ratio that it said it had negotiated with the Colorado marketplace before CMS's approval of that ratio. However, there is no evidence showing that the Colorado marketplace provided input about the 50/50 cost allocation ratio in the discussions with HCPF or CMS.

The Colorado marketplace allowed the 50/50 cost allocation ratio to be used, but it performed little or no oversight of the development of the allocation rates. Also, the Colorado marketplace did not maintain documentation for the cost allocation ratio. This ratio may not have produced an equitable allocation of costs based on the benefits received by each entity from the SES. However, we are not questioning the costs associated with this finding because CMS approved the revised CAP even though it was based on an arbitrary ratio rather than on expected transactions or expected program population.

THE COLORADO MARKETPLACE ALLOWED SHARED ELIGIBILITY SYSTEM COSTS TO BE ALLOCATED TO THE INCORRECT COST ALLOCATION PLAN PERIOD

The Colorado marketplace allowed SES costs totaling \$2,110,378 to be improperly allocated to it by HCPF. These costs were incurred, either entirely or in part, during the *initial* CAP period but were allocated using the cost allocation ratio in effect for the *revised* CAP period.

Federal Requirements

For a cost to be allowable, it must be allocable to a Federal award (2 CFR part 225, Appendix A, § C.1). A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to that cost objective in accordance with the relative benefits received (2 CFR part 225, Appendix A, § C.3).

Shared Eligibility System Costs Incurred in the Initial Cost Allocation Period That Were Improperly Allocated to the Colorado Marketplace

Costs Not Properly Allocated to the Colorado Marketplace by the Colorado Department of Health Care Policy & Financing

From the inception of the Colorado marketplace in 2011 through June 30, 2016, the Colorado marketplace paid HCPF a total of \$6,751,990 (Appendix D) for the development and implementation of the SES. On the basis of the 50/50 cost allocation ratio in effect for the revised CAP period, \$4,641,612 in SES costs incurred during that period was allocated to the Colorado marketplace. However, the Colorado marketplace incurred an additional \$2,110,378 in SES costs, either entirely or in part, during the *initial* CAP period. The Colorado marketplace allowed these costs to be improperly allocated because it allowed use of the 50/50 cost allocation ratio in effect for the *revised* CAP period. This report seeks to make the Colorado marketplace aware of the potential impact of any incorrect allocations of costs associated with any future Federal grant awards.

This amount consisted of:

- SES costs totaling \$351,048 that were incurred entirely in the initial CAP period but were allocated to the Colorado marketplace using the 50/50 cost allocation ratio in effect for the revised CAP period and
- SES costs totaling \$1,759,330 (extracted from project costs that were incurred in both the initial and revised CAP periods) for projects in which costs were incurred in the initial CAP period but for which the project costs were allocated to the Colorado marketplace using the 50/50 cost allocation ratio in effect for the revised CAP period.

Improperly Allocated Costs Incurred Entirely During the Initial Cost Allocation Plan Period

The Colorado marketplace allowed SES costs to be allocated to it by HCPF based on a cost allocation ratio that did not apply to the period during which the costs were incurred. We identified \$351,048 in SES costs incurred entirely during the *initial* CAP period that should have been allocated to the Colorado marketplace using the cost allocation ratio in effect for that *initial* CAP period but that were instead allocated using the 50/50 cost allocation ratio in effect for the *revised* CAP period. Table 2 below breaks out the specific projects or purposes to which these improperly allocated SES costs were assigned.

Table 2: Improperly Allocated Costs Based on the Revised CAP for SES Costs That Were Incurred Entirely During the Initial CAP Period

| Improperly Allocated Costs | Purpose |
|-----------------------------------|--|
| \$290,024 | Plug and Play Capabilities With the Exchange ¹⁶ (the Colorado marketplace) |
| \$59,000 | Implementation Infrastructure |
| \$2,024 | Paper Application Development ¹⁷ |
| \$351,048 | Total |

Improperly Allocated Costs Incurred During Both Cost Allocation Plan Periods

In addition to the categories of SES costs identified in Table 2, which could be assigned entirely to the initial CAP period, the Colorado marketplace had projects for which it incurred other SES costs in both the initial and revised CAP periods. As identified in Table 3 on the following page, the Colorado marketplace allowed SES costs that it had incurred during the initial allocation period to be allocated to it using the 50/50 ratio from the revised allocation period.

¹⁶ “Plug and Play Capabilities With the Exchange” was the name given to a project designed to build automated interfaces between the Colorado marketplace and HCPF.

¹⁷ The purpose of the “Paper Application Development” project was to process paper applications for enrollment (as part of the manual enrollment process in the first enrollment period) into health insurance plans sold by the Colorado marketplace.

Table 3: Improperly Allocated Costs Based on the Revised CAP for SES Costs That Were Partially Incurred During the Initial CAP Period

| Improperly Allocated Costs | Purpose |
|-----------------------------------|--|
| \$323,695 | Master Project: Colorado Benefits Management System (CBMS) Shared Eligibility System Phase I |
| \$323,695 | CBMS Shared Eligibility System Phase I—Eligibility |
| \$323,695 | CBMS Shared Eligibility System Phase I—Interfaces |
| \$323,695 | CBMS Shared Eligibility System Phase I—Program Eligibility and Application Kit |
| \$323,695 | CBMS Shared Eligibility System Phase I—Security/Single Sign on |
| \$140,855 | CBMS Shared Eligibility System—C4HCO and HCPF—Phase II |
| \$1,759,330 | Total |

The \$1,759,330 in SES costs was incurred during the *initial* CAP period, but the Colorado marketplace allowed all of the \$1,759,330 to be allocated to it on the basis of the cost allocation ratio in effect for the *revised* CAP period.

Inadequate Internal Controls

The Colorado marketplace did not have adequate internal controls to ensure that SES costs were properly allocated to it by HCPF using the cost allocation ratios in effect for the appropriate CAP period. HCPF first charged the Colorado marketplace for the marketplace’s share of the SES costs after the revised CAP had been approved. However, some of the SES

costs charged to the Colorado marketplace had in fact been incurred during the initial CAP period. The Colorado marketplace lacked controls to ensure that those SES costs incurred during the initial CAP period were allocated to it on the basis of the initial cost allocation ratio rather than the revised cost allocation ratio.

RECOMMENDATIONS

We recommend that the Colorado marketplace:

- develop and implement a cost allocation methodology that is based on relative benefits received by the Colorado marketplace and that is based on updated, better data regarding expected transactions and program population as the data become available;
- develop and implement written policies, reinforced by adequate internal controls, that explain how to develop a CAP based on relative benefits received, expected transactions, and expected population; how to provide formal input to HCPF and CMS during the development of cost allocation ratios; and how to adequately document the development of those ratios; and
- develop and implement written policies and procedures to ensure that future Federal grant award costs are allocated to it in the appropriate period in accordance with Federal requirements.

AUDITEE COMMENTS

In written comments on our draft report, the Colorado marketplace neither agreed nor disagreed with our recommendations but described corrective actions that it had implemented or planned to implement to address those recommendations. According to the Colorado marketplace, these corrective actions included developing a CAP that was approved by CMS in September 2017, developing processes to evaluate proposed allocation methodologies, and modifying accounting processes and procedures to more accurately track costs.

The Colorado marketplace's written comments appear in their entirety as Appendix E.

APPENDIX A: AUDIT SCOPE AND METHODOLOGY

SCOPE

We reviewed the NGAs associated with the \$183.7 million that CCIIO awarded to the Colorado marketplace—three establishment grants and a post-award amendment to the third of the three grants—beginning in FY 2012 and extending through the third quarter of 2016 (February 22, 2012, through June 30, 2016). Because CMS permitted States to request NCEs for the use of establishment grant funds after January 1, 2015, for activities not related to the operational costs of their marketplaces and because the Colorado marketplace requested and received an NCE,¹⁸ we extended our audit period to June 30, 2016.

We limited our review of internal controls to the systems and procedures for allocating and claiming costs to establishment grants and to Medicaid. We obtained an understanding of how the Colorado marketplace and HCPF developed the cost allocation methodologies.

We previously reported on the Colorado marketplace's expenditure of establishment grant funds (A-07-14-02801, Dec. 27, 2016). We are still conducting audit work on several aspects of the Colorado marketplace's operations and plan to report on them separately.

Our audit work included site visits to the Colorado marketplace and HCPF offices in Denver, Colorado.

METHODOLOGY

To accomplish our objective, we:

- reviewed applicable Federal and State laws, regulations, and guidance;
- reviewed the Colorado marketplace's establishment grant application packages;
- reviewed CCIIO's Funding Opportunity Announcements and NGA terms and conditions;
- reviewed IAPD version 4, which HCPF submitted to CMS, as well as CMS's approval document dated January 2, 2013, which started the initial CAP period;
- reviewed IAPD version 7, which HCPF submitted to CMS, as well as CMS's approval document dated September 30, 2014, which started the revised CAP period;
- reviewed SES costs provided to us by the Colorado marketplace and HCPF and assigned those costs to the initial CAP period, the revised CAP period, or both;

¹⁸ CMS, *FAQs on the Use of 1311 Funds and No-Cost Extensions* (Mar. 2014). CMS approved the Colorado marketplace's request for an NCE in November 2014.

- interviewed CCIIO officials to gain an understanding of guidance they provided to HCPF and the Colorado marketplace concerning the CAPs;
- interviewed HCPF and Colorado marketplace officials and reviewed the SES MOU between the two entities to gain an understanding of how the SES costs were allocated and used;
- reviewed the Colorado marketplace’s policies and procedures for financial management;
- interviewed Colorado marketplace officials to gain an understanding of their accounting systems and internal controls;
- interviewed Colorado marketplace officials to gain an understanding of enrollment statistics available to the marketplace for individuals determined eligible for and enrolled in QHPs, Medicaid, or CHIP;
- obtained expenditure general ledgers for FYs 2012 through 2016 (through June 2016) that were related to the three establishment grants as well as the post-award amendment to the third of the three grants;
- obtained and reviewed the Colorado marketplace’s actual enrollment figures for QHP from October 1, 2013, through July 31, 2016;
- obtained and reviewed HCPF’s actual enrollment figures for Medicaid and CHIP from October 1, 2013, through July 31, 2016; and
- discussed the preliminary results of our review with Colorado marketplace officials on September 12, 2017.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

APPENDIX B: FEDERAL GRANTS TO STATES FOR PLANNING, ESTABLISHING, AND EARLY OPERATION OF MARKETPLACES

CCIIO used a phased approach to provide States with resources for planning and implementing marketplaces. CCIIO awarded States and one consortium of States planning and establishment grants, including early innovator cooperative agreements and two types of marketplace establishment cooperative agreements.

PLANNING AND ESTABLISHMENT GRANTS

CCIIO awarded planning and establishment grants¹⁹ to assist States with initial planning activities related to the potential implementation of the marketplaces. States could use these funds in a variety of ways, including to assess current IT systems; determine the statutory and administrative changes needed to build marketplaces; and coordinate streamlined eligibility and enrollment systems across State health programs, including Medicaid and CHIP. In September 2010, CCIIO awarded grants in amounts up to a maximum of \$1 million per State to 49 States and the District of Columbia. (Alaska did not apply for a planning and establishment grant.)

EARLY INNOVATOR COOPERATIVE AGREEMENTS

CCIIO awarded early innovator cooperative agreements²⁰ to States to provide them with incentives to design and implement the IT infrastructure needed to operate marketplaces. These cooperative agreements rewarded States that demonstrated leadership in developing cutting-edge and cost-effective consumer-based technologies and models for insurance eligibility and enrollment for marketplaces. The “early innovator” States received funding to develop IT models, “building universally essential components that can be adopted and tailored by other States.” In February 2011, CCIIO awarded 2-year early innovator cooperative agreements to six States and one consortium of States. Awards ranged from \$6.2 million (Maryland) to \$59.9 million (Oregon).

¹⁹ CCIIO, *State Planning and Establishment Grants for the Affordable Care Act’s Exchanges*, Funding Opportunity Number: IE-HBE-10-001, Jul. 29, 2010.

²⁰ CCIIO, *Cooperative Agreements to Support Innovative Exchange Information Technology Systems*, Funding Opportunity Number: TBA, Oct. 29, 2010. In February 2011, CMS announced that it had awarded seven early innovator cooperative agreements. The cooperative agreements totaled \$249 million.

MARKETPLACE ESTABLISHMENT COOPERATIVE AGREEMENTS

CCIIO designed establishment cooperative agreements²¹ to support States' progress toward establishing marketplaces. Establishment cooperative agreements awarded through December 31, 2014, were available for States seeking (1) to establish a State-based marketplace, (2) to build functions that a State elects to operate under a State partnership marketplace, and (3) to support State activities to build interfaces with the federally facilitated marketplace. Cooperative agreement funds were available for approved and permissible establishment activities and could include startup year expenses to allow outreach, testing, and necessary improvements during the startup year. In addition, a State that did not have a fully approved State-based marketplace on January 1, 2013, could have continued to qualify for and receive establishment cooperative agreement awards in connection with its activities related to establishment of the federally facilitated marketplace or State partnership marketplace, subject to certain eligibility criteria. States were eligible for multiple establishment cooperative agreements.

There were two categories of establishment cooperative agreements: Level One and Level Two. Level One establishment cooperative agreements were open to all States, whether they were (1) participating in the federally facilitated marketplace (including States collaborating with the federally facilitated marketplace through the State partnership model) or (2) developing a State-based marketplace. All States could have applied for Level One establishment cooperative agreements, including those that previously received exchange planning and establishment grants. Level One award funds were available for up to 1 year after the date of the award.

Level Two establishment cooperative agreements were available to States, including those that previously received exchange planning and establishment grants. Level Two establishment cooperative agreement awards provided funding for up to 3 years after the date of the award. These awards were available to States that could demonstrate that they had (1) the necessary legal authority to establish and operate a marketplace that complies with Federal requirements available at the time of the application, (2) established a governance structure for the marketplace, and (3) submitted an initial plan discussing long-term operational costs of the marketplace.

States could have initially applied for either a Level One or a Level Two establishment cooperative agreement. Those that had received Level One establishment cooperative agreements could have applied for another Level One establishment cooperative agreement by a subsequent application deadline. Level One establishment grantees also could have applied for a Level Two establishment cooperative agreement provided the State had made sufficient

²¹ CCIIO, *Cooperative Agreement to Support Establishment of State-Operated Health Insurance Exchanges*, Funding Opportunity Number: IE-HBE-11-004, November 29, 2011, and *Cooperative Agreement to Support Establishment of the Affordable Care Act's Health Insurance Exchanges*, Funding Opportunity Number: IE-HBE-12-001, Dec. 6, 2013.

progress in the initial Level One establishment project period and was able to satisfy the eligibility criteria for a Level Two establishment cooperative agreement.

In determining award amounts, CCIIO looked for efficiencies and considered whether the proposed budget would be sufficient, reasonable, and cost effective to support the activities proposed in the State's application. According to the Funding Opportunity Announcement, the cooperative agreements funded only costs for establishment activities that were integral to marketplace operations and meeting marketplace requirements, including those defined in existing and future guidance and regulations issued by HHS. A marketplace must use ACA, section 1311(a), funds consistent with ACA requirements and related guidance from CCIIO.

States must have ensured that their marketplaces were self-sustaining beginning on January 1, 2015 (ACA § 1311(d)(5)(A)).

**APPENDIX C: FEDERAL GRANTS AWARDED FOR ESTABLISHING AND EARLY OPERATION
OF THE COLORADO MARKETPLACE AS OF DECEMBER 31, 2016**

The following table summarizes the grants awarded by CCIIO to support the establishing and early operation of the Colorado marketplace and expenditures allocated to these grants.

| Grant Number | Award Period²² | Award Type | Award Total | Expenditures |
|---------------------------|---|-------------------|----------------------|----------------------|
| HBEIE120111 | February 22, 2012– April 15, 2013 | First Level One | \$17,951,000 | \$17,951,000 |
| HBEIE120131 | September 27, 2012– January 15, 2014 | Second Level One | 43,486,747 | 43,486,747 |
| HBEIE130169 ²³ | July 9, 2013– June 30, 2016 | Level Two | 122,301,350 | \$122,301,350 |
| Total | | | \$183,739,097 | \$183,739,097 |

Note: The Colorado marketplace has fully expended all of the Federal grant funds that have been awarded to it.

²² The award period for each grant number includes NCEs.

²³ This award period and its award total include the post-award amendment of the Level Two grant that was awarded in December 2014.

APPENDIX D: SHARED ELIGIBILITY SYSTEM COSTS ALLOCATED TO THE COLORADO MARKETPLACE

| Purpose | Total Costs | Costs Allocated to the Correct CAP Period | Costs Allocated to the Incorrect CAP Period |
|---|--------------------|--|--|
| December 2014 MOU/Revenue Agreement: total \$4,707,439 (Payment #1) | \$1,025,415 | \$676,391 | \$349,024 |
| December 2014 MOU/Revenue Agreement: total \$4,707,439 (Payment #2) | \$2,902,024 | \$1,140,670 | \$1,761,354 |
| December 2014 MOU/Revenue Agreement: total \$4,707,439 (Payment #3) | \$780,000 | \$780,000 | 0 |
| Open Enrollment Year 3 System Changes | \$1,871,811 | \$1,871,811 | 0 |
| User Acceptance Testing Open Enrollment Year 3 | \$75,000 | \$75,000 | 0 |
| March 2016 Release Override Project (researching status of project) | \$97,740 | \$97,740 | 0 |
| Totals | \$6,751,990 | \$4,641,612 | \$2,110,378 |

Connect for Health Colorado appreciates the opportunity to respond to the recommendations in the final report of the Office of Inspector General (OIG) titled *Colorado Did Not Always Comply With Federal Requirements When Expending Federal Establishment Grant Funds Allocated For Its Shared Eligibility System Costs*. We take all audit recommendations seriously and use it as an opportunity to improve our processes. The following is our response to the recommendations contained in the OIG report.

Recommendation: Develop and implement a cost allocation methodology that is based on relative benefits received by the Colorado marketplace and that is based on an updated, better data regarding expected transactions and program population as the data become available.

Beginning in 2015, HCPF and the Colorado marketplace started jointly developing a cost allocation plan to provide a robust methodology for allocating costs between the two organizations. This work culminated with a CMS approved cost allocation plan (CAP) in September 2017. The CAP categorizes costs into 26 categories and uses 7 different evidence based allocation methodologies depending upon the type of cost. These allocation methodologies are based on SES eligibility determinations, appointment data, staffing and random moment time study data. In conjunction with the CAP, a contract was entered into with HCPF in January 2018 that provides the guidance for how costs are to be shared between the two organizations.

Recommendation: Develop and implement written policies, reinforced by adequate internal controls, that explain how to develop a CAP based on relative benefits received, expected transactions, and expected population; how to provide formal input to HCPF and CMS during the development of cost allocation ratios; and how to adequately document the development of these ratios.

Through the creation of the CAP over the last two years, the Colorado marketplace developed processes to evaluate proposed allocation methodologies in accordance with the relative benefits received by the two organizations. Additionally, communication channels were developed with HCPF and CMS providing the Colorado marketplace formal input as we progressed through the approval process of the CAP. These processes will be formalized into written policies/procedures that can be used in future cost allocation projects.

Recommendation: Develop and implement written policies and procedures to ensure that future Federal grant award costs are allocated to it in the appropriate period in accordance with Federal requirements.

The Colorado marketplace has modified its accounting processes and procedures to assure costs associated with a funding source are accurately tracked and recorded in the proper period.

Sincerely,

/Kevin N. Patterson/

Kevin N. Patterson, MURP, MPA
Chief Executive Officer
March 14, 2018