

January 25, 2018

Michael Cohen, Director
California Department of Finance
915 L Street
Sacramento, CA 95814

Dear Mr. Michael Cohen,

In accordance with the State Leadership Accountability Act (SLAA), the California Health Benefit Exchange submits this report on the review of our internal control and monitoring systems for the biennial period ending December 31, 2017.

Should you have any questions please contact Thien Lam, Program Integrity Director, at (916) 228-8600, Thien.Lam@covered.ca.gov.

BACKGROUND

Under the federal Patient Protection and Affordable Care Act (Affordable Care Act) signed into law in March 2010, states were required to decide whether to create a state-based health insurance exchange or participate in the federal multi-state health insurance exchange. California elected to establish a state-based health insurance exchange. In 2010, state law [Government Code 100500 et seq.; Chapter 655, Statutes of 2010 (Perez) and Chapter 659, Statutes of 2010 (Alquist)] was enacted to implement the provisions of the Affordable Care Act and to “reduce the number of uninsured Californians by creating an organized, transparent marketplace for Californians to purchase affordable, quality health care coverage, to claim available tax credits and cost-sharing subsidies, and to meet the personal responsibility requirements imposed under the federal act.” This legislation established the California Health Benefit Exchange (Exchange).

To achieve the goals outlined in legislation, the Exchange identified the mission to increase the number of insured Californians, improve health care quality, lower costs, and reduce health disparities through an innovative, competitive marketplace that empowers consumers to choose the health plan and providers that give them the best value. To achieve this mission, the Exchange adopted the following six values:

1. **Consumer-focused:** At the center of the Exchange’s efforts are the people it serves, including patients and their families, and small business owners and their employees. The Exchange will offer a consumer-friendly experience that is accessible to all Californians, recognizing the diverse cultural, language, economic, educational, and health status needs of those we serve.
2. **Affordability:** The Exchange will provide affordable health insurance while assuring quality and access.
3. **Catalyst:** The Exchange will be a catalyst for change in California’s health care system, using its market role to stimulate new strategies for providing high-quality and affordable health care, promoting prevention and wellness, and reducing health disparities.
4. **Integrity:** The Exchange will earn the public’s trust through its commitment to accountability, responsiveness, transparency, speed, agility, reliability, and cooperation.
5. **Partnership:** The Exchange welcomes partnerships, and its efforts will be guided by working with consumers, providers, health plans, employers and other purchasers, government partners, and other stakeholders.

6. Results: The impact of the Exchange will be measured by its contributions to expanding coverage and access, improving health care quality, promoting better health and health equity, and lowering costs for all Californians.

ONGOING MONITORING

As the head of California Health Benefit Exchange, Peter V. Lee, Executive Director, is responsible for the overall establishment and maintenance of the internal control and monitoring systems.

EXECUTIVE MONITORING SPONSOR(S)

The executive monitoring sponsor responsibilities include facilitating and verifying that the California Health Benefit Exchange internal control monitoring practices are implemented and functioning as intended. The responsibilities as the executive monitoring sponsor(s) have been given to: Virginia Corbitt, Program Oversight and Compliance Branch Chief.

MONITORING ACTIVITIES

The Exchange has implemented a comprehensive bi-annual enterprise risk management assessment and reporting process that is designed to assist leadership with strategic planning and decision-making; provide an effective and efficient way to evaluate and act on risks and opportunities; and communicate information on ways to improve internal controls and performance in all program areas. The risk assessment report is reviewed by leadership for potential impact on Covered California's strategic pillars and key initiatives, and divisional performance goals and objectives. The Exchange manages its risks through coordinated activities; such as, corrective actions plans and mitigation strategies, aligned enterprise goals, and evaluation of opportunities to ensure risks are managed effectively, efficiently, and coherently across the Exchange.

The Internal Audit Services Unit uses the risk assessment report, among other processes and techniques, to develop its Annual Audit Plan. The Annual Audit Plan uses a risk-based approach to identify and prioritize audits based upon specific risk factors related to the quality of internal controls and the estimated liability and level of risk exposure to the Exchange. The Internal Audit Services Unit implements the Annual Audit Plan by using a systematic, disciplined approach to evaluate and improve the effectiveness and efficiency of operations and provides a level of assurance that internal controls are operating as intended.

Additionally, there is collaboration with all program areas to improve system and operational efficiencies for consumers who apply for health coverage and enroll in health plans through the Exchange. For example, ongoing User Acceptance Testing is performed on the California Healthcare Eligibility, Enrollment and Retention System's (CalHEERS) key functionalities prior to implementation to help reduce the number of critical system issues. Post-Implementation Reviews are also performed to improve operational efficiencies and compliance with federal and state regulations and mandates.

ADDRESSING VULNERABILITIES

As risks or vulnerabilities are identified and reported, corrective action plans are developed, tracked, and updated. This is primarily overseen through the Enterprise Risk Management process and through the internal and external audit coordination process. In addition to the internal audits and services performed by the Internal Audit Services Unit, the Exchange is federally-required to have annual independent external financial and programmatic audits performed. In addition, all new and emerging critical risks identified from routine operations are reported bi-weekly to executive and senior

leadership. From these processes, all risks, findings, and opportunities for improvement are addressed with the corrective action plans and mitigation strategies.

When a risk has been identified, the impacted program area assigns a primary contact who can address and potentially mitigate the program area of its vulnerability. Resources are then allocated to implement the corrective actions and mitigation strategies. The primary contact provides ongoing reports on the status of the corrective actions, anticipated timelines, and provides support to confirm the corrective actions have been fully implemented.

COMMUNICATION

An Enterprise Risk Management infrastructure was developed to help ensure that monitoring roles, activities, and results are shared and communicated throughout the organization. Management and staff were trained on the risk assessment process to gain an understanding of the risk categories, ranking values, reporting process, and the development of corrective action plans and mitigation strategies.

As part of the reporting process, divisional managers are required to provide an impact statement for each risk identified. Development of the required impact statements requires consideration of the likelihood of occurrence, consequence of risk events if they are realized, an evaluation of current internal controls, and identification of the monitoring procedures to be performed to mitigate the risk. When a corrective action plan is developed, it is tracked and monitored on an ongoing basis.

The risks that are identified by divisional managers are recorded into a comprehensive risk assessment database, which is used to prepare divisional risk management reports that are ultimately shared with managers and senior leadership.

The risk management reports provide a summary of the risk results, identifies the specific performance goals being impacted, and communicates risks that cross between the various divisions. The report also identifies and addresses prior audit findings to help management prioritize their divisional risks.

ONGOING MONITORING COMPLIANCE

The California Health Benefit Exchange has implemented and documented the ongoing monitoring processes as outlined in the monitoring requirements of California Government Code sections 13400-13407. These processes include reviews, evaluations, and improvements to the California Health Benefit Exchange systems of controls and monitoring.

RISK ASSESSMENT PROCESS

The following personnel were involved in the California Health Benefit Exchange risk assessment process: Executive Management, Middle Management, Front Line Management, and Staff.

RISK IDENTIFICATION

The Exchange's Enterprise Risk Management process embodies the widely accepted Committee of Sponsoring Organizations of the Treadway Commission (COSO) model for evaluating internal controls over the effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations. For example, the COSO enterprise risk management framework defines essential components, suggests a common language, and provides clear direction and guidance for enterprise risk management.

To conduct our enterprise risk assessment for the 2016-2017 reporting period, the Exchange considered the results of our risk management reports, internal audit reviews, external audit results performed by independent audit firms, and ongoing executive risk and issue reviews. Specifically:

- Risks are identified through our Enterprise Risk Management process. Our risk assessment process requires all divisions to report new, emerging, and ongoing risks that may impact the Exchange's strategic pillars, performance goals, and mission.
- Throughout the risk-based audit process, from planning stages to issuance of final reports, the Internal Audit Services Unit uses multiple auditing techniques that include, but are not limited to, interviews, observations, questionnaires, meetings, document and policy reviews, and group discussions to identify risks.
- The Exchange has been audited by federal and state oversight entities, including the Office of Inspector General and the California State Auditors, had site reviews performed by the Centers for Medicare and Medicaid and the Office of Management and Budget, and had independent external financial and programmatic audits performed. Observations and findings are given consideration for process improvements and corrective action plans. The observations and findings may be reported and prioritized as risks by management.
- In the event issues are identified during Post Implementation Reviews, each issue or risk is categorized and prioritized for resolution.

The risks identified in this report were derived from the aforementioned processes. These risks were primarily identified by division management using an enterprise risk assessment tool. As mentioned previously, risks are identified and updated bi-annually by each division's management and reported in the risk management database. Each risk is also assessed to determine if it impacts the Exchange's strategic pillars, performance goals and objectives, and reviewed by senior leadership.

Additionally, the audits and reviews capture a wide range of operational and programmatic functions, which affords the Exchange's leadership a more comprehensive risk assessment perspective and opportunity to efficiently prioritize risks for mitigation efforts.

RISK RANKING

Each division ranks their risks based on the likelihood of occurrence and impact to the Exchange's mission, strategic pillars, budget, program management, and other business objectives. As previously noted, management has been provided the training and tools to guide them in ranking the value of their risks as High, Medium, or Low. The Enterprise Risk Management Unit compiles the information, prepares management reports, and prioritizes the tops risks based on description, category, factor, and score for leadership review.

RISKS AND CONTROLS

RISK: OPERATIONS -EXTERNAL-POLITICAL, REPUTATION, MEDIA

There is continued uncertainty at the federal level surrounding the future of the Patient Protection and Affordable Care Act and the impact of changes in federal policies on consumer enrollment and affordability of care.

The Exchange ended the year with major changes in federal policy which created significant uncertainty potentially impacting premiums and the rate of the uninsured. Causes for uncertainty include:

- Elimination in 2017 of direct funding for federal cost-sharing reduction reimbursement payments.

- Repeal of the individual mandate, effective 2019.
- Short-term/limited duration and associated health plans.

In 2017, the federal Department of Health and Human Services (DHHS) eliminated direct funding for cost-sharing subsidy reimbursement payments. In anticipation of this policy decision, the Exchange created a workaround to assure continual health plan participation and protect consumers from resulting increased premiums. This workaround helped keep premiums stable by adding a cost-sharing reduction surcharge only for on-exchange Silver-tier plans to limit the impact on consumers who do not receive cost-sharing reduction subsidies. Because the surcharge was only applied to on-exchange Silver-tier plans, nearly four out of five consumers have seen their premiums stay the same or decrease. A recent Exchange analysis found that the net monthly premiums for the over 1 million Californians who received financial help are on average 10 percent lower than what new and renewing consumers paid last year.

The Tax Cuts and Jobs Act eliminated the individual mandate penalty starting in 2019. Independent analysis projects drops in enrollment, and because those dropping coverage are likely to be healthier individuals, premium increases for those who remain enrolled could range from 8 to 13 percent depending on state-specific factors.

DHHS issued proposed regulations expanding the ability of employers to participate in association health plans. DHHS will also be issuing proposed regulations allowing short-term/limited-duration health plans. The creation of association health plans selling across state lines and the potential expansion of short-term/limited-duration health plans could siphon healthy consumers from the common risk pool of the individual markets, worsen the risk mix, and raise premiums for those who remain covered.

CONTROL A

State-based approaches are making a difference and the Exchange will continue to remain focused on doing the work of fostering a competitive market that works for California's consumers. The Exchange will be nimble and proactive in the face of potential changes to federal or state policy, while seeking to continue to share with policy-makers in California, and nationally, the lessons and experiences of a market that is working.

RISK: OPERATIONS -INTERNAL-FI\$CAL IMPLEMENTATION, MAINTENANCE, OR FUNCTIONALITY

California Government Code Section 15849.22 (b) (1) requires that all state departments and agencies shall use the FI\$Cal System. The FI\$Cal system shall replace any existing central or departmental systems duplicative of the functionality of the FI\$Cal system.

The change in the financial reporting systems from California State Accounting & Reporting System (CalSTARS) to the implementation of the Financial Information System for California (FI\$Cal) could potentially create risk for the Exchange:

- Without proper User Acceptance Testing to understand how the system and workflows were created, we cannot be assured that the processes and ability to transact are successful. Data entry transactions may not be processed timely and efficiently.
- If the conversion of data from CalSTARS to FI\$Cal is not successful, it will require manual data entry and additional temporary staff to help with keying in the data.
- CalSTARS will no longer be available after December 12, 2018, to continue to process the Exchange's Small Business transactions. We are currently seeking methods to process these payments prior to the closure of CalSTARS.
- The availability of reports will be limited which will have an impact on compliance and financial reporting.

- Our control agencies, the Department of General Services and State Treasurer Office, inability to allow the system to go live by July 1, 2018 may affect how the Exchange will process payments. The Exchange's process cannot be finalized without receiving advance notice of the necessary information.

The Exchange's transition to FISCAL must be complete since we will not have access to the current legacy system (CalSTARS). FISCAL instructions and resources to assist with conversion spreadsheets are limited, leaving the Exchange with spreadsheets that have continuous errors. These errors will not allow for full conversion due to the lack of FISCAL personnel and available written resources. Staff of the Exchange are unable to retrieve answers and gain an understanding of proper processes. These resources are needed to adequately document new processes. The inability to access and educate staff on the actual live system prevents staff from finalizing processes and procedures before going live. Resources to assist the Exchange staff with learning how FISCAL is configured and creating processes are not centralized. It is inefficient to search for processes and training material across multiple websites and multiple departments. The training materials are inconsistent; do not contain robust material and are not user friendly.

The FISCAL Project team is hiring a contractor who has actual experience in the FISCAL project and system to help navigate questions that are affecting our ability to get answers to solve our workflow and process issues. Management has consulted with other agencies who have fully implemented FISCAL to acquire "Lessons Learned" to assist in making informed decisions. Regular internal discussions on lessons learned and information gathered regarding work processes are made to ensure the staff is educated and trained to complete daily work assigned. It is imperative that workflows are updated on a regular basis to help ensure a smooth implementation of the system. We continue to plan for an increase in staff as well as special equipment needs.

CONTROL A

The FISCAL Project team is hiring a contractor with actual experience in both the FISCAL project and system to help navigate our questions that are affecting our ability to obtain information to solve our workflow and process issues. Management has consulted with other agencies who have fully implemented FISCAL to acquire "Lessons Learned" to assist management and staff in making informed decisions. Regular internal discussions on lessons learned and information gathered regarding work processes are conducted to help ensure staff are educated and trained to complete the daily work assigned. It is imperative that workflows are being updated on a regular basis to ensure smooth implementation of the system when it goes live. We continue to plan for an increase in staff as well as special equipment needs.

CONTROL B

If, with all the controls outlined in Control A, the Exchange still experiences challenges with implementation of FISCAL, then Exchange staff will continue to work outside the FISCAL system for critical, time sensitive procurement and contracting needs by using current paper process, CAL Card as the payment mechanism, and pay CAL Card through a Revolving Fund Check; staff would then have to go back and manually rekey all these transaction into the FISCAL system. A possible solution to help mitigate purchasing needs through 2018 is to add a central supply area.

RISK: OPERATIONS -EXTERNAL-STAFF—RECRUITMENT, RETENTION, STAFFING LEVELS

The Exchange continues to experience barriers that reduce our ability to recruit, hire, and retain qualified staff. These barriers could impact the ability to carry out our mission.

External factors have impacted our ability to effectively and efficiently achieve our staffing objectives. Civil

service hiring processes and control agency examinations; recruitment and hiring requirements are lengthy, require minimum qualifications be met for positions (e.g. IT classifications), which do not require equivalent experience, training and education as in the private sector. Similarly, the State's pay scales are less competitive than the private sector.

Internal factors have also affected our ability to recruit, hire, and retain staff. Funding is needed to build and maintain a social media campaign to help broaden our candidate pool for hard-to-fill positions by using one or more social media platforms (e.g. LinkedIn, Indeed, Monster, etc.).

The Exchange is limited in leveraging technology platforms that support modern recruitment trends. Absent thereof, the Exchange is not competitive with the private sector showcasing us as an employer of choice.

CONTROL A

Since January 2017, the Exchange has implemented the following controls to help mitigate the risk:

- Released an updated employment website. The website advertises our vacancies, job fairs, events, exams, and guides candidates on applying for positions within the Exchange.
- Participated in more than 20 recruitment events.
- Implemented a Recruitment Questionnaire for applicants via Survey Monkey and upon interviewing to gauge how applicants learned about the Exchange vacancies.
- Release of recruitment opportunities to diversity partners and attendees at recruitment events.
- Implemented efficiencies to reduce the hiring process timeline.
- Hired a highly experienced recruiter.
- Launched new recruitment flyers and materials with pay differential information targeting Program Technician classifications and bilingual certified candidates.
- Developed HR Weekly Announcement

RISK: OPERATIONS -INTERNAL-OVERSIGHT, MONITORING, INTERNAL CONTROL SYSTEMS

Gaps and vulnerabilities were identified in the current Oversight and Monitoring Plan that may affect the Exchange's ability to timely identify and mitigate risks.

The Exchange adopted enterprise policies and procedures to implement an Oversight and Monitoring Plan. The plan established a consolidated repository for conducting internal oversight and monitoring activities along with the implementation of best practices as a continuously evolving and integrated part of the Exchange's day-to-day operations. The plan was designed to foster accountability and transparency, mitigate the risk of systemic vulnerabilities going undetected, and reduce the frequency of operational problems. Specifically, each operating division within the Exchange must have established detailed guidelines, policies, procedures, control measures, and clearly defined roles and responsibilities to help achieve the Exchange's objectives.

However, while we do closely monitor internal controls, there have been a few instances wherein inefficiencies and other opportunities for program and process improvements were not timely identified by management. In addition, it became evident that the roles and responsibilities for oversight and monitoring were not clearly defined among the different program areas. This risk is primarily due to the rapid implementation timeline to launch the new marketplace in response to the Affordable Care Act.

Without a more detailed oversight and monitoring program, the Exchange is at risk of not effectively and efficiently monitoring internal controls, quickly identifying operational inefficiencies and vulnerabilities timely, and prioritizing corrective actions to address compliance issues with federal and state laws and regulations.

The program will help deter fraud, waste, abuse activities and help ensure records are accurate and reliable.

CONTROL A

To address this risk and improve our processes, the Oversight and Monitoring Plan, which was accepted by our federal oversight agency, is being updated and will be submitted to the Centers for Medicare and Medicaid Services as required of all State-Based Marketplaces. The Oversight and Monitoring Plan will delineate how program areas are strengthening operational effectiveness, maintaining compliance with laws and regulations, providing accurate and reliable records, and preventing and detecting instances of fraud, waste, and abuse.

Updating the Oversight and Monitoring Plan will increase organizational transparency and understanding about the importance of oversight and monitoring activities including self-assessment tasks.

CONCLUSION

The California Health Benefit Exchange strives to reduce the risks inherent in our work and accepts the responsibility to continuously improve by addressing newly recognized risks and revising controls to prevent those risks from happening. I certify our internal control and monitoring systems are adequate to identify and address current and potential risks facing the organization.

Peter V. Lee, Executive Director

CC: California Legislature [Senate (2), Assembly (1)]
California State Auditor
California State Library
California State Controller
Director of California Department of Finance
Secretary of California Government Operations Agency