

VERMONT EDUCATION HEALTH INITIATIVE, INC.

AUDIT REPORT

JUNE 30, 2016 AND 2015

VERMONT EDUCATION HEALTH INITIATIVE, INC.
AUDIT REPORT
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JUNE 30, 2016 AND 2015

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Independent Auditor's Report

Board of Directors
Vermont Education Health
Initiative, Inc.
52 Pike Drive
Berlin, Vermont 05602

Report on the Financial Statements

We have audited the accompanying financial statements of the Vermont Education Health Initiative, Inc., as of and for the years ended June 30, 2016 and 2015 as listed in the Table of Contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 Vermont Education Health Initiative, Inc.'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 Vermont Education Health Initiative, Inc.'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

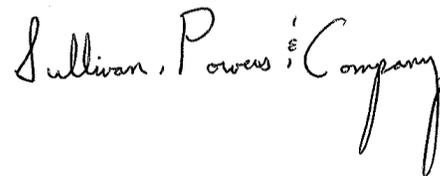
In our opinion, the financial statements referred to previously present fairly, in all material respects, the financial position of the Vermont Education Health Initiative, Inc. as of June 30, 2016 and 2015 and the results of its operations and its cash flows for the years then ended in accordance with 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 on pages 3 through 7 and the financial information listed as Tables 1 and 2 in the table of contents 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.

September 19, 2016
Montpelier, Vermont
VT Lic. #92-000180

A handwritten signature in cursive script that reads "Sullivan, Powers & Company". The signature is written in black ink and is positioned to the right of the date and address information.

VERMONT EDUCATION HEALTH INITIATIVE, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

For The Year Ended June 30, 2016

The Vermont Education Health Initiative (VEHI) is a large group purchaser of health care and related benefit plans for school district employees and retirees in Vermont. VEHI was incorporated on July 1, 1996 under the Nonprofit Corporation Act and as such all revenue is exempt from Federal and State income taxes under Internal Revenue Code Section 115. VEHI is managed jointly by the Vermont School Boards Insurance Trust (VSBIT) and the Vermont-NEA (VT-NEA).

VEHI's mission is to offer high-quality employee benefit options and related services in a cost effective manner on behalf of its members. As a member organization, VEHI plays an active role in all areas of health care and related benefit plan design, financing, marketing, risk management, wellness, consumer education and customer service.

Effective June 7, 2013 VEHI was approved as an Intermunicipal Insurance Association by the Vermont Department of Financial Regulation.

Fiscal 2016 Highlights and Overall Financial Position

During the year ending June 30, 2016, VEHI, partnered with Blue Cross Blue Shield of Vermont and Northeast Delta Dental to provide health insurance to 276 and dental insurance coverage to 194 schools and related organizations.

VEHI's program contributions totaled \$284,851,209 in 2016, an increase of \$9 million from 2015. VEHI holds \$2.4 million in contribution receivable and \$2.19 million in prepaid contributions as of June 30, 2016. VEHI earned \$701,826 in investment income in 2016, an increase of \$323,248 from 2015. VEHI also received \$759,856 from Blue Cross Blue Shield of Vermont in value added and administrative performance revenue.

VEHI's overall net position increased by \$7.6 million in 2016: from \$33.8 to \$41.45 million. The Health Program's net position increased by \$7.4 million. The Dental Program's net position increased by \$195 thousand. This follows a \$1.5 million decrease in overall net position in 2015.

The Financial Statements

VEHI's financial statements are a series of reports that detail financial information using enterprise fund accounting and financial reporting. They are prepared in accordance with GASB 34 and GASB 37. VEHI uses the accrual basis method of accounting in preparing its financial statements.

The statement of revenues, expenses, and changes in net position presents the results of VEHI's operations. The statement reports all revenues and expenses, and reconciles the beginning and end of year net position balances.

The statement of net position includes all the Corporation's assets and liabilities. The statement also presents the balance of assets in excess of liabilities, or net position.

The statement of cash flows supplements these statements providing relevant information about cash receipts and payments to the Corporation.

FINANCIAL INFORMATION

SUMMARY OF REVENUE AND EXPENSES

	<u>2016</u>	<u>2015</u>
Operating Revenues:	<u>\$285,611,065</u>	<u>\$276,551,347</u>
Operating Expenses:		
Net Change in Health/Dental Claims Paid and Reserved	248,591,581	247,859,126
Capitation-Health	3,442,794	3,410,279
Reinsurance & Administration-Health/Dental	17,044,800	18,507,729
Assessments	5,844,687	5,634,118
Other Expenses	<u>3,764,248</u>	<u>2,972,774</u>
Total Operating Expenses	<u>278,688,110</u>	<u>278,384,026</u>
Operating Income	<u>6,922,955</u>	<u>(1,832,679)</u>
Non-operating Revenue		
Total Investment Activity	<u>694,374</u>	<u>333,845</u>
Change in Net Position	7,617,329	(1,498,834)
Net Position - Beginning of Year	<u>33,838,172</u>	<u>35,337,006</u>
Net Position - End of Year	<u>\$ 41,455,501</u>	<u>\$ 33,838,172</u>

Revenues

VEHI's fiscal 2016 operations resulted in an increase in net position of \$7.6 million, following the 2015 decrease of \$1.5 million. For FY16 VEHI raised health rates by 4.5%. This followed a 4.5% increase for fiscal year 2015. All revenues for 2016 are considered operating revenues except for investment income. VEHI earned \$285.6 million in revenues versus \$278.7 million in total expenses in 2016. Revenues come primarily from program contributions which increased \$9.4 million for health in 2016. Dental contributions decreased \$315 thousand as overall the rates for the Dental Program were reduced by 6.1% on average.

Investments are held at the Peoples United Bank and with the Vanguard Group in the form of money market accounts and government and corporate bonds. VEHI earned \$550 thousand in interest and dividends in 2016, up from \$527 thousand in 2015. The bond market performance improved in 2016. VEHI recorded a positive market change of \$152 thousand as compared to a negative market change of \$149 thousand in 2015.

Expenses

VEHI's largest expense is the actual claims paid by Blue Cross Blue Shield of Vermont and Northeast Delta Dental. These are reimbursed directly by VEHI and totaled \$248.6 million in 2016, \$700 thousand over the 2015 claims expense. Capitation expense increased slightly by \$33 thousand, from \$3.41 million to \$3.44 million.

Reinsurance and administrative expenses paid to Blue Cross Blue Shield of Vermont and Northeast Delta Dental make up \$17 million of total expenses in 2016, a \$1.5 million decrease from 2015. Beginning with FY15, the Blue Cross Blue Shield of Vermont administrative fee includes a contribution to its reserve funds as approved by the Green Mountain Care Board.

In 2013 State and Federal Assessments to VEHI were \$3.48 million. Each year assessments have continued to increase totaling \$5.6 million by FY15. In FY16 assessments increased to \$5.8 million. Federal assessments totaled \$1.7 million, Vermont assessments totaled \$4.1 million, and out of state assessments were \$21,983.

VEHI incurred other expenses in the amount of \$3.76 million, a \$791 thousand increase from 2015. In 2016, VEHI contracted with Remedy Analytics to bring additional expertise and analytical tools to the pharmacy arena. With support from Remedy, BCBSVT renegotiated on VEHI's behalf a three year contract with Express Scripts, resulting in increased cost savings for VEHI members. With additional data on pharmacy utilization and pricing available from Remedy's technology, VEHI will work with BCBSVT to further reduce pharmacy spend without negatively impacting membership. This new service accounted for \$500 thousand of VEHI's FY16 increase to other expenses. VEHI offers the PATH (Planned Action Toward Health) Program to all members. This expense, in the amount of \$1.85 million, makes up the majority of other expenses. VEHI's primary objective is to control related claims costs while helping members to obtain health and dental care in the most effective manner. PATH, VEHI's wellness program, facilitates this objective. Administrative services are provided to VEHI by VSBIT and the VT-NEA. For the year ending June 30, 2016 VEHI incurred expenses of \$1.053 million in accordance with administrative services contracts with these entities. The remaining \$359 thousand of other expenses was paid directly to vendors by VEHI.

CONDENSED FINANCIAL INFORMATION

SUMMARY OF NET POSITION

	<u>2016</u>	<u>2015</u>
Assets:		
Cash and investments	\$53,345,637	\$44,673,363
Other Assets	<u>7,560,263</u>	<u>8,421,797</u>
Total Assets	<u>\$60,905,900</u>	<u>\$53,095,160</u>
Liabilities:		
Deferred Revenue	\$ 2,193,788	\$ 1,487,748
Other Payables	<u>17,256,611</u>	<u>17,769,240</u>
Total Liabilities	<u>19,450,399</u>	<u>19,256,988</u>
Net Position:		
Unrestricted Net Position	<u>41,455,501</u>	<u>33,838,172</u>
Total Net Position	<u>41,455,501</u>	<u>33,838,172</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$60,905,900</u>	<u>\$53,095,160</u>

Assets

Cash and investments are held at the Peoples United Bank and at the Vanguard Group in the form of money market accounts and government and corporate bonds.

Other assets totaling \$7.56 million consists mainly of a working fund deposit in the amount of \$4.98 million maintained by Blue Cross Blue Shield of Vermont. This account is a non interest bearing cash account used to pay claims and is estimated to be one week's claims payable. VEHI also held \$2.4 million in contribution receivable as of June 30.

Liabilities

VEHI collected \$2.19 million in contribution for fiscal year 2017 prior to June 30, 2016 due to payment timing by our member schools. This is an increase of \$706 thousand over last year.

Other payables of \$17.2 million consist primarily of claims payable to Blue Cross Blue Shield of Vermont and Northeast Delta Dental in the amount of \$16.2 million. Also included; \$669 thousand due for state and federal assessments, \$5,875 in accrued administration fees to process the claims payable, and \$360 thousand due to other vendors.

Economic Factors

For fiscal year 2017, the Department of Financial Regulation approved a 7.9% health rate increase. This follows a 4.5% increase for 2016.

Dental insurance contributions were decreased by 2.34% on average for fiscal year 2017, following a 6.1% decrease for fiscal year 2016.

Requests for Information

The financial report is designed to provide a general overview of VEHI's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the President, Vermont Education Health Initiative, Inc., 52 Pike Drive, Berlin, VT 05602.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
STATEMENT OF NET POSITION
JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
<u>ASSETS</u>		
Current Assets:		
Cash - Note 2	\$ 478,456	\$ 3,086
Investments - Note 2	52,867,181	44,670,277
Accrued Interest Receivable	85,723	91,006
Contributions Receivable	2,400,000	2,309,704
Working Fund Deposit - Note 3	4,985,109	4,670,674
Other Receivables - Note 4	67,051	417,147
Advance to the Vermont State Teachers Retirement System - Note 5	0	931,666
Prepaid Expenses - Note 6	<u>22,380</u>	<u>1,600</u>
Total Current Assets	<u>60,905,900</u>	<u>53,095,160</u>
TOTAL ASSETS	<u>\$ 60,905,900</u>	<u>\$ 53,095,160</u>
<u>LIABILITIES AND NET POSITION</u>		
Current Liabilities:		
Accounts Payable	\$ 360,062	\$ 244,260
Assessments Payable	669,199	537,355
Unearned Revenue - Note 7	2,193,788	1,487,748
Claims Payable - Note 8	16,221,475	16,974,046
Reserve for Unallocated Loss Adjustment Expenses	<u>5,875</u>	<u>13,579</u>
Total Current Liabilities	<u>19,450,399</u>	<u>19,256,988</u>
Total Liabilities	<u>19,450,399</u>	<u>19,256,988</u>
Net Position:		
Unrestricted Net Position	<u>41,455,501</u>	<u>33,838,172</u>
Total Net Position - Note 9	<u>41,455,501</u>	<u>33,838,172</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 60,905,900</u>	<u>\$ 53,095,160</u>

The accompanying notes are an integral part of this financial statement.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
Operating Revenues:		
Health Contributions	\$ 277,686,297	\$ 268,319,313
Dental Contributions	7,164,912	7,479,791
Value Payment Revenue - Note 10	756,356	751,243
Administrative Performance Revenue - Note 10	3,500	1,000
	<u>285,611,065</u>	<u>276,551,347</u>
Total Operating Revenues		
Operating Expenses:		
Net Change in Health Claims Paid and Reserved - Note 11	242,488,800	241,822,971
Net Change in Dental Claims Paid and Reserved - Note 11	6,102,781	6,036,155
Reinsurance and Administration - Health	16,461,857	17,951,337
Capitation - Health	3,442,794	3,410,279
Assessments - Note 12	5,844,687	5,634,118
Program Administration - Dental	582,943	556,392
General and Administrative Expenses - Note 13	1,911,911	1,452,843
Wellness Grants and Expenses	1,852,337	1,519,931
	<u>278,688,110</u>	<u>278,384,026</u>
Total Operating Expenses		
Operating Income/(Loss)	<u>6,922,955</u>	<u>(1,832,679)</u>
Nonoperating Revenues/(Expenses):		
Investment Income	701,826	378,578
Investment Fees	(7,452)	(44,733)
	<u>694,374</u>	<u>333,845</u>
Total Nonoperating Revenues/(Expenses)		
Change in Net Position	7,617,329	(1,498,834)
Net Position - Beginning of Year	<u>33,838,172</u>	<u>35,337,006</u>
Net Position - End of Year	<u>\$ 41,455,501</u>	<u>\$ 33,838,172</u>

The accompanying notes are an integral part of this financial statement.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
Cash Flows from Operating Activities:		
Cash Received from Health and Dental Contributions	\$ 285,466,953	\$ 274,540,911
Cash Received from Value Payment Revenue	756,356	812,411
Cash Received from Administrative Performance Revenue	3,500	101,500
Cash Paid for Health and Dental Claims	(249,344,152)	(244,958,880)
Cash Paid for Reinsurance, Capitation and Administration	(20,097,255)	(22,373,695)
Cash Paid for Assessments	(5,712,842)	(5,571,548)
Cash Paid for General and Administrative Expenses	(1,868,855)	(1,351,811)
Cash Paid for Wellness Grants and Expenses	(1,848,319)	(1,519,931)
	<u>7,355,386</u>	<u>(321,043)</u>
Cash Flows from Noncapital Related Financing Activities:	<u>0</u>	<u>0</u>
Cash Flows from Capital and Related Financing Activities:	<u>0</u>	<u>0</u>
Cash Flows from Investing Activities:		
Net Increase in Long-Term Investments	(8,196,904)	(1,058,264)
Increase in Working Fund Deposit	(314,435)	(49,000)
Decrease in Advance to the Vermont State Teachers Retirement System	931,666	1,068,334
Cash Received from Interest and Dividends	707,109	382,792
Cash Paid for Investment Fees	(7,452)	(44,733)
	<u>(6,880,016)</u>	<u>299,129</u>
Net Increase/(Decrease) in Cash and Cash Equivalents	475,370	(21,914)
Cash and Cash Equivalents, Beginning of Year	<u>3,086</u>	<u>25,000</u>
Cash and Cash Equivalents, End of Year	<u>\$ 478,456</u>	<u>\$ 3,086</u>
Reconciliation of Operating Income/(Loss) to Net Cash Provided/(Used) by Operating Activities		
Operating Income/(Loss)	\$ 6,922,955	\$ (1,832,679)
Changes in Operating Assets and Liabilities:		
Decrease/(Increase) in Contributions Receivable	(90,296)	(1,188,900)
Decrease/(Increase) in Other Receivables	350,096	(250,424)
Decrease/(Increase) in Prepaid Expenses	(20,780)	(350)
Increase/(Decrease) in Accounts Payable	115,802	58,160
Increase/(Decrease) in Assessments Payable	131,844	62,571
Increase/(Decrease) in Unearned Revenue	706,040	(69,293)
Increase/(Decrease) in Claims Payable	(752,571)	2,900,244
Increase/(Decrease) in Reserve for Unallocated Loss Adjustment Expenses	<u>(7,704)</u>	<u>(372)</u>
Net Cash Provided/(Used) by Operating Activities	<u>\$ 7,355,386</u>	<u>\$ (321,043)</u>

The accompanying notes are an integral part of this financial statement.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Vermont Education Health Initiative, Inc. (herein, “VEHI”) was established in 1996 by the Vermont National Education Association (VNEA) and the Vermont School Boards Insurance Trust (VSBIT) to provide schools and related organizations with health insurance and other related coverage.

VEHI is considered an Intermunicipal Insurance Association under Vermont law and is regulated by the Vermont Department of Financial Regulation. Membership in VEHI is limited to municipal school districts and their instrumentalities and agencies.

School Districts joining VEHI must remain members for a minimum of one year. A member may withdraw from VEHI after that time by giving ninety (90) day notice. VEHI currently provides health coverage to 276 schools and related organizations and dental coverage to 194 schools and related organizations.

The major accounting policies followed by VEHI are presented below to assist the reader in evaluating the financial statements.

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies adopted by VEHI conform to generally accepted accounting principles (GAAP) as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing accounting and financial reporting principles. The following is a summary of the more significant accounting policies employed in the preparation of these financial statements.

VEHI reports itself as a business-type activity as defined in GASB 34. Business-type activities are financed in whole or in part by fees charged to external parties. Business-type activities distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses result from providing services and producing and delivering goods in connection with VEHI’s principal ongoing operations. The principal operating revenues of VEHI includes health contributions and fees received from providing services. Operating expenses include health claims paid and the costs of providing services and operating all programs. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The financial statements of VEHI are reported using the accrual basis of accounting. Revenues are recognized in the period in which the applicable coverage is provided and expenses are recognized in the period in which they are incurred, regardless of when the related cash flow takes place.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 1:
(Cont'd)

The financial statements of VEHI are reported using the economic resources measurement focus. This means that all assets and liabilities associated with the operation of VEHI (whether current or noncurrent) are included on the balance sheet (or statement of net position). Fund equity (i.e., total net position) is segregated into net investment in capital assets (if applicable); restricted net position; and unrestricted net position. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total position.

The presentation of financial statements in conformity with generally accepted accounting principles 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

VEHI incorporated as a Nonprofit Corporation under the Nonprofit Corporation Act. All their revenue is exempt from Federal and State income taxes under Internal Revenue Code Section 115 which pertains to political subdivisions.

Health and Dental contributions and other fees are recognized in the period of coverage.

Health insurance contributions are determined by an agreement between VEHI and Blue Cross and Blue Shield of Vermont and approved by the Vermont Department of Financial Regulation and the Green Mountain Care Board. Blue Cross and Blue Shield pays the actual health claims filed by members of VEHI and requests reimbursement by VEHI. The agreement provides for stop loss coverage of \$700,000 per individual and 120% of expected claims on an annual basis.

Dental insurance contributions for participating school districts are individually determined through an agreement with Northeast Delta Dental and an independent consultant. Northeast Delta Dental pays the actual dental claims filed by members of VEHI and requests reimbursement by VEHI.

Cash includes amounts in demand deposits. Cash does not include cash equivalents in the investment accounts.

VEHI uses the allowance method for uncollectible accounts. The allowance for doubtful accounts as of June 30, 2016 and 2015 is \$0.

Investments with readily determinable fair values are reported at their fair values. Unrealized gains and losses are included in revenue.

VEHI categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 2: CASH AND INVESTMENTS

Cash and Investments as of June 30, 2016 and 2015 consist of the following:

	<u>2016</u>	<u>2015</u>
Cash - Deposits with Financial Institutions	\$ <u>478,456</u>	\$ <u>3,086</u>
Investments:		
Investments - Mutual Funds *	42,167,456	31,619,523
Investments - Corporate Bonds	10,699,725	10,731,054
Investments - Government Bonds	<u>0</u>	<u>2,319,700</u>
Total Investments	<u>52,867,181</u>	<u>44,670,277</u>
Total Cash and Investments	<u>\$53,345,637</u>	<u>\$44,673,363</u>

At June 30, 2016, VEHI's operating account had a book balance of \$478,456 and a bank balance of \$512,414. At June 30, 2015, the book balance was \$3,086 and bank balance was \$24,942.

- * At June 30, 2016, \$20,896,385 was invested in the Federated Institutional Prime Obligations Fund and \$21,271,071 was invested in the Vanguard Short-Term Bond Index Fund which includes bonds by various issuers.
- * At June 30, 2015, \$13,820,428 was invested in the Fidelity Government Money Market Fund and \$17,799,095 was invested in the Vanguard Short-Term Bond Index Fund which includes bonds by various issuers.

VEHI's Board of Directors has established an investment policy which indicates which types of investments VEHI can own. VEHI has two classes of investments, Class A and Class B. Class A funds can only be invested in cash equivalents that have a maturity that will meet the projected cash flow needs on a month to month basis. Class B funds can only be invested in near cash equivalents having a maturity of five (5) years or less at the time of purchase and/or money market mutual funds.

Investments of operating funds shall be limited to insured bank deposits, repurchase agreements, U.S. Treasury or agency securities, money market funds, and commercial paper rated A-1 or P-1 or better by Standard & Poor's and Moody's, respectively, or funds which invest in similar instruments. Additionally, with respect to fixed income investments, the minimum average credit quality of these investments shall be investment grade (Standard & Poor's BBB; Moody's Baa) or higher. No one issuer, except the U.S Treasury or a sponsored agency, can exceed 10% of the market value of the portfolio. No one debt issue, except those of the U.S. Treasury or a sponsored agency, can exceed 5% of the market value of the portfolio.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 2:
(Cont'd)

Effective June 7, 2013, VEHI re-organized as an Intermunicipal Insurance Association under Regulation I-90-1. This statute limits how operating funds may be invested. VEHI's investment policy is in compliance with these restrictions.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, VEHI will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party.

The custodial credit risk for investments is the risk that, in the event of failure of the counter-party (e.g. broker-dealer) to a transaction, VEHI will not be able to recover the value of its investments or collateral securities that are in possession of another party.

The account with the People's United Bank requires minimum daily balances and the residual amounts are transferred to People's United Bank Investment Services and are invested in cash equivalents.

VEHI's mutual funds are open-ended and are not exposed to custodial credit risk. VEHI's corporate and government bonds are not exposed to custodial credit risk.

The custodial credit risk for cash deposits is as follows:

	2016		2015	
	Book Balance	Bank Balance	Book Balance	Bank Balance
Insured/(FDIC)	\$ 250,000	\$ 250,000	\$ 3,086	\$ 24,942
Uninsured, Uncollateralized	228,456	262,414	0	0
Total	\$ 478,456	\$ 512,414	\$ 3,086	\$ 24,942

The difference between the book and the bank balance is due to reconciling items such as deposits in transit and outstanding checks.

Interest Rate Risk

Interest rate risk is the risk that changes in market rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 2:
(Cont'd)

Information about the sensitivity of the fair values of VEHI's investments to market interest rate fluctuations is provided by the following table that shows the distribution of VEHI's investments by maturity. Mutual funds are shown at their weighted average maturity and the corporate and government bonds are shown at their actual maturity.

2016				
Investment Type	Remaining Maturity			Total
	One Year Or Less	1 to 2 Years	2 to 3 Years	
	Mutual Funds	\$ 42,167,456	\$ 0	
Corporate Bonds	2,219,536	8,480,189	0	10,699,725
Total	\$ 44,386,992	\$ 8,480,189	\$ 0	\$ 52,867,181

2015				
Investment Type	Remaining Maturity			Total
	One Year Or Less	1 to 2 Years	2 to 3 Years	
	Mutual Funds	\$ 31,619,523	\$ 0	
Corporate Bonds	0	2,252,812	8,478,242	10,731,054
Government Bonds	2,319,700	0	0	2,319,700
Total	\$ 33,939,223	\$ 2,252,812	\$ 8,478,242	\$ 44,670,277

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented as follows are the actual ratings as of June 30, 2016 and 2015. The ratings displayed are those of Standard and Poors.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

June 30, 2016					
	Government Bonds	Corporate Bonds	Mutual Funds	Total	Percent of Total
AA	\$ 0	\$ 3,520,332	\$ 0	\$ 3,520,332	7%
A	0	4,781,433	0	4,781,433	9%
BBB	0	2,397,960	0	2,397,960	5%
Not rated	0	0	42,167,456	42,167,456	79%
	\$ 0	\$ 10,699,725	\$ 42,167,456	\$ 52,867,181	100%

June 30, 2015					
	Government Bonds	Corporate Bonds	Mutual Funds	Total	Percent of Total
AA	\$ 0	\$ 4,270,265	\$ 0	\$ 4,270,265	10%
A	0	5,961,474	0	5,961,474	13%
BBB	0	499,315	0	499,315	1%
Not rated	0	0	31,619,523	31,619,523	71%
Exempt	2,319,700	0	0	2,319,700	5%
	\$ 2,319,700	\$ 10,731,054	\$ 31,619,523	\$ 44,670,277	100%

Concentration of Credit Risk

The limitations on the amount that can be invested in any one issuer are disclosed previously in the investment policy. No investments, other than mutual funds, represented more than 5% of total investments at June 30, 2016 and June 30, 2015 respectively.

Fair Value

VEHI has the following recurring fair value measurements as of June 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Quoted Market Prices (Level 1 Inputs):		
Government Bonds	\$ 0	\$ 2,319,700
Corporate Bonds	10,699,725	10,731,054
Mutual Funds	<u>42,167,456</u>	<u>31,619,523</u>
Investment at Fair Value	<u>\$ 52,867,181</u>	<u>\$ 44,670,277</u>

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 3: WORKING FUND DEPOSIT

The Working Fund Deposit consists of a non-interest bearing cash account in the amount of \$4,985,109 and \$4,670,674 at June 30, 2016 and 2015, respectively, that is maintained at Blue Cross and Blue Shield. This imprest account is used to pay claims by VEHI's claims processors. These are estimated to be one week's claims payable.

Note 4: OTHER RECEIVABLES

Other Receivables at June 30, 2016 include \$64,571 due from Blue Cross and Blue Shield of Vermont for Value Payment Revenue. Also included in Other Receivables is \$2,480 due from others.

Other Receivables at June 30, 2015 include \$62,486 and \$350,341 due from Blue Cross and Blue Shield of Vermont for Value Payment Revenue and a Federal Transitional Reinsurance overpayment refund, respectively. Also included in Other Receivables is \$4,320 due from others.

Note 5: ADVANCE TO THE VERMONT STATE TEACHERS RETIREMENT SYSTEM

During fiscal year 2014, VEHI advanced \$2,000,000 to the Vermont State Teachers Retirement System. During fiscal year 2015, VEHI advanced an additional \$400,000 and recouped a total of \$1,468,334. The remaining balance of \$931,666 was completely recouped from subsidies from the Center for Medicare Service and from manufacturer's brand discounts net of the partner pharmacy company's cost to administer the pharmacy program. The balance as of June 30, 2016 is \$0.

Note 6: PREPAID EXPENSES

Prepaid expenses of \$22,380 as of June 30, 2016 represents insurance payments for fiscal year 2017 coverage.

Prepaid expenses of \$1,600 as of June 30, 2015 represents deposits for 2016 conferences.

Note 7: UNEARNED REVENUE

Unearned revenue of \$2,193,788 as of June 30, 2016 represents \$2,144,478 of health insurance contributions and \$49,310 of dental insurance contributions received in advance for fiscal year 2017.

Unearned revenue of \$1,487,748 as of June 30, 2015 represents \$1,447,773 of health insurance contributions and \$39,975 of dental insurance contributions received in advance for fiscal year 2016.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 8: CLAIMS PAYABLE

VEHI establishes claims liabilities based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Estimated amounts of reinsurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Claims liabilities were computed using a variety of actuarial and statistical techniques. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made.

The claims payable of \$16,221,475 as of June 30, 2016 represents \$3,737,890 of health claims and \$103,197 of dental claims due to Blue Cross and Blue Shield of Vermont and Northeast Delta Dental for benefits actually paid by them as of June 30, 2016 but not reimbursed by VEHI as of that date and it also includes \$12,159,688 of health claims and \$220,700 of dental claims incurred as of June 30, 2016 but not paid by Blue Cross and Blue Shield of Vermont and Northeast Delta Dental as of that date.

The claims payable of \$16,974,046 as of June 30, 2015 represents \$4,250,164 of health claims and \$0 of dental claims due to Blue Cross and Blue Shield of Vermont and Northeast Delta Dental for benefits actually paid by them as of June 30, 2015 but not reimbursed by VEHI as of that date and it also includes \$12,484,882 of health claims and \$239,000 of dental claims incurred as of June 30, 2015 but not paid by Blue Cross and Blue Shield of Vermont and Northeast Delta Dental as of that date.

Note 9: NET POSITION

For the year ended June 30, 2016, VEHI has a reserve of net position which represents an operating surplus of \$41,455,501. This surplus will be used to help fund the health program to the reinsurance attachment point and to minimize future rate increases.

For the year ended June 30, 2015, VEHI has a reserve of net position which represents an operating surplus of \$33,838,172. This surplus will be used to help fund the health program to the reinsurance attachment point and to minimize future rate increases.

Note 10: VALUE PAYMENT REVENUE/ADMINISTRATIVE PERFORMANCE REVENUE

The Value Payment Revenue of \$756,356 and \$751,243 for 2016 and 2015, respectively, represent amounts received from Blue Cross and Blue Shield of Vermont as a service credit for value added service provided to its members by VEHI which ultimately reduces the amount of administration provided by Blue Cross and Blue Shield of Vermont. This service credit revenue is equal to \$2.91 per contract per month for the years ending June 30, 2016 and June 30, 2015, respectively.

The Administrative Performance Revenue of \$3,500 and \$1,000 for 2016 and 2015, respectively, represent penalties per an agreement between Blue Cross and Blue Shield of Vermont and VEHI. Blue Cross and Blue Shield of Vermont is subject to penalties for failure to provide high levels of services as described in the agreement.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 11: CLAIMS PAID AND PAYABLE

An analysis of the net change in health and dental claims paid and payable is as follows:

	<u>2016</u>	<u>2015</u>
Health Claims Paid (Net of Recoveries)	\$243,326,268	\$238,805,425
Payable - End of Year	15,897,578	16,735,046
Less: Payable - Beginning of Year	<u>(16,735,046)</u>	<u>(13,717,500)</u>
Net Change in Health Claims Paid and Reserved	<u>\$242,488,800</u>	<u>\$241,822,971</u>
	<u>2016</u>	<u>2015</u>
Dental Claims Paid (Net of Recoveries)	\$ 6,017,884	\$ 6,153,457
Payable - End of Year	323,897	239,000
Less Payable - Beginning of Year	<u>(239,000)</u>	<u>(356,302)</u>
Net Change in Dental Claims Paid and Reserved	<u>\$ 6,102,781</u>	<u>\$ 6,036,155</u>

Note 12: ASSESSMENTS

For the year ending June 30, 2016 and 2015, assessments included \$5,694,428 and \$5,487,933, respectively, paid to Blue Cross and Blue Shield of Vermont for State and Federal mandated insurance fees. In 2016 and 2015, \$91,889 and \$88,661, respectively, was paid to the Department of the Treasury for the annual PCOR Fee. In 2016 and 2015, \$58,370 and \$57,524, respectively, was also paid to Northeast Delta Dental for the State HCCA assessment. These fees are for various State programs as follows:

During fiscal year 2015, the State consolidated two programs, the Vermont Information Technology Leaders (VITL), and the Vermont Health Care Claims Assessment (HCCA). VITL fees of .199% were effective October 1, 2009 and HCCA fees of .8% were effective October 1, 2011 on claims paid and capitation payments for Vermont residents. As consolidated programs, the State of Vermont assesses a fee of .999%.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 12:
(Cont'd)

Vermont Blueprint for Health (Blueprint) – This is a State of Vermont program that pays providers based on performance and the amount paid to providers is determined by the National Committee for Quality Assurance ratings. The State of Vermont maintains a table that provides a per member per month equivalent for the results reported.

Federal Transitional Reinsurance – Beginning January 1, 2014, this is a Federal per member fee paid by Blue Cross and Blue Shield of Vermont and passed through to VEHI. The fee charged by Blue Cross and Blue Shield of Vermont to VEHI was \$4.46 and 2.96 per month during fiscal year 2016 and 2015, respectively, for each non-Medicare and non-Medicaid member only.

Patient Centered Outcomes Research (PCOR) – This is a Federal fee on all memberships of \$2 per member per year for policies ending in the fiscal year 2014. Thereafter, the fee will increase at the cost of medical inflation and will sunset in 2019. This assessment went into effect with the Patient Protection and Affordable Care Act of 2010. The fee for fiscal year 2016 and 2015 was \$2.17 and \$2.08, respectively, per member.

Assessment fees paid to Blue Cross and Blue Shield of Vermont and Northeast Delta Dental for State and Federal mandated insurance fees were as follows:

	<u>2016</u>	<u>2015</u>
HCCA	\$2,313,411	\$2,238,948
Blueprint	1,807,758	1,287,997
Federal Transitional Reinsurance	1,609,646	1,996,324
PCOR	91,889	88,661
Out of State Assessments	<u>21,983</u>	<u>22,188</u>
Totals	<u>\$5,844,687</u>	<u>\$5,634,118</u>

Note 13: GENERAL AND ADMINISTRATIVE EXPENSES

Most of the Vermont Education Health Initiative’s administrative services are provided by VSBIT and VNEA. For the year ending June 30, 2016 and 2015, VEHI incurred general and administrative expenses of \$1,053,048 and \$1,034,651, respectively, in accordance with an administrative service contract with both VSBIT and VNEA.

The remaining \$858,863 and \$418,192 for the year ending June 30, 2016 and 2015, respectively, was paid directly to vendors by VEHI.

Note 14: RISK MANAGEMENT

VEHI is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. VEHI maintains commercial insurance coverage through a local broker. Management believes such coverage is sufficient to preclude any significant uninsured losses to VEHI. Settled claims have not exceeded this coverage in any of the past three fiscal years.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

Note 15: AFFILIATED ORGANIZATIONS

The Vermont School Boards Insurance Trust, Inc. and the Vermont National Education Association (VNEA) jointly manage the Vermont Education Health Initiative (VEHI). VEHI contracts with VSBIT to provide management, wellness and accounting services. VEHI paid VSBIT \$777,612 and \$759,765 for these services in 2016 and 2015, respectively. Furthermore, the President for VSBIT is also the president for VEHI. Also, VSBIT's Corporate Secretary is a VSBIT board member and VEHI's Corporate Secretary is a VEHI board member. VEHI contracts with VNEA to provide program and member services. VNEA was paid \$275,436 and \$274,886 for services in 2016 and 2015, respectively.

VEHI contracts with VNEA on an annual basis. Beginning July 1, 2014, VEHI has a five (5) year contract with VSBIT for services. After the end of the initial five year term, the contract automatically renews for two (2) additional two (2) year terms. The contract can be cancelled by either party at the end of the initial term and each additional term. The fee for the 2016 year is \$777,612, paid quarterly. The fee is subject to adjustment each year.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
CLAIMS DEVELOPMENT INFORMATION
JUNE 30, 2016

This table illustrates how VEHI's earned revenues (net of reinsurance) and investment income compare to related costs of loss (net of loss assumed by reinsurers) and other expenses assumed by VEHI for the last ten (10) years. The rows of the table are defined as follows: (1) This line shows the gross of each fiscal year's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's reinsurance and capitation premiums. (3) This line shows the net of each fiscal year's earned contribution revenues and investment revenues. (4) This line shows each fiscal year's other operating costs of VEHI including overhead and claims expense not allocable to individual claims. (5) This line shows VEHI's incurred claims and allocated claims adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year). (6) This section of rows shows the cumulative amounts paid as of the end of successive years for each policy year. (7) This section of rows shows how each policy year's incurred claims increased or decreased as of the end of successive years. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (8) This line compares the latest reestimated incurred claims amount to the amount originally established (line 5) and shows whether this latest estimate of claims cost is greater or less than originally determined.

See Disclaimer in the Independent Auditor's Report.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
CLAIMS DEVELOPMENT INFORMATION
JUNE 30, 2016

	<u>2006/07</u>	<u>2007/08</u>	<u>2008/09</u>	<u>2009/10</u>	<u>2010/11</u>	<u>2011/12</u>	<u>2012/13</u>	<u>2013/14</u>	<u>2014/15</u>	<u>2015/16</u>
1. Gross Contribution and Investment Revenues	\$ 191,087,452	\$ 205,017,767	\$ 212,833,652	\$ 218,361,905	\$ 225,812,610	\$ 235,828,317	\$ 245,024,843	\$ 267,907,885	\$ 276,177,685	\$ 285,553,035
2. Reinsurance and Capitation Premiums	14,635,070	16,317,050	15,293,409	14,213,997	14,477,657	14,393,643	14,099,987	7,197,659	7,033,506	6,796,007
3. Net Earned Required Contribution and Investment Revenues	176,452,382	188,700,717	197,540,243	204,147,908	211,334,953	221,434,674	230,924,856	260,710,226	269,144,179	278,757,028
4. Unallocated Expenses	12,850,415	13,683,477	16,239,632	17,662,429	18,305,420	20,460,172	19,257,731	20,531,034	22,783,885	22,548,115
5. Estimated Incurred Claim and Expense, End of Policy Year	153,585,712	161,748,892	179,901,386	188,872,285	201,192,844	217,723,716	224,835,668	234,301,608	247,689,300	249,855,083
6. Paid (cumulative) as of:										
End of Policy Year	142,210,521	148,300,779	164,704,900	171,622,903	185,636,051	201,055,904	205,662,095	220,227,806	230,715,254	233,633,608
One Year Later	153,585,712	161,748,892	179,901,386	188,872,285	201,192,884	217,723,716	224,283,092	234,471,434	246,425,798	
7. Reestimated Incurred Claims:										
End of Policy Year	153,585,712	161,748,892	179,901,386	188,872,285	201,192,884	217,723,716	224,835,668	234,301,608	247,689,300	249,855,083
One Year Later	153,585,712	161,748,892	179,901,386	188,872,285	201,192,844	217,723,716	224,283,092	234,471,434	246,425,798	
8. Increase/(Decrease) in Estimated Incurred Claims from End of Policy Year	0	0	0	0	0	0	(552,576)	169,826	(1,263,502)	N/A

See Disclaimer in the Independent Auditors Report.

VERMONT EDUCATION HEALTH INITIATIVE, INC.
RECONCILIATION OF CLAIMS LIABILITIES
FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

The schedule below presents the changes in health and dental claims liabilities:

	Health		Dental	
	2016	2015	2016	2015
Unpaid Claims and Allocated Claim Adjustment Expenses at Beginning of the Year	\$ <u>16,735,046</u>	\$ <u>13,717,500</u>	\$ <u>239,000</u>	\$ <u>356,302</u>
Incurred Claims and Claim Adjustment Expenses:				
Provision for Insured Events of the Current Year	243,735,989	241,645,942	6,119,094	6,043,358
Increase/(Decrease) in Provision for Insured Events of Prior Years	<u>(1,247,189)</u>	<u>177,029</u>	<u>(16,313)</u>	<u>(7,203)</u>
Total Incurred Claims and Claim Adjustment Expenses	<u>242,488,800</u>	<u>241,822,971</u>	<u>6,102,781</u>	<u>6,036,155</u>
Payments:				
Claims and Allocated Claim Adjustment Expenses Attributable to Insured Events of the Current Year	227,838,411	224,910,896	5,795,197	5,804,358
Claims and Allocated Claim Adjustment Expenses Attributable to Insured Events of Prior Years	<u>15,487,857</u>	<u>13,894,529</u>	<u>222,687</u>	<u>349,099</u>
Total Payments	<u>243,326,268</u>	<u>238,805,425</u>	<u>6,017,884</u>	<u>6,153,457</u>
Total Unpaid Claims and Allocated Claim Adjustment Expenses at End of the Year	\$ <u><u>15,897,578</u></u>	\$ <u><u>16,735,046</u></u>	\$ <u><u>323,897</u></u>	\$ <u><u>239,000</u></u>

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