

CONNECTICUT HEALTH FOUNDATION, INC.

FINANCIAL STATEMENTS

DECEMBER 31, 2012 AND 2011

CONNECTICUT HEALTH FOUNDATION, INC.

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Independent Auditors' Report

To the Board of Directors
Connecticut Health Foundation, Inc.

We have audited the accompanying financial statements of Connecticut Health Foundation, Inc. (the Foundation), which comprise the statements of financial position as of December 31, 2012, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements. The financial statements of the Foundation as of December 31, 2011 were audited by other auditors, whose report dated August 10, 2012 expressed an unqualified opinion on those statements.

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.

Auditors' 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 auditors' 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 auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Connecticut Health Foundation, Inc., as of December 31, 2012, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Blum, Shapiro & Company, P.C.

West Hartford, Connecticut
April 10, 2013

CONNECTICUT HEALTH FOUNDATION, INC.
STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
ASSETS		
Cash and cash equivalents	\$ 1,415,481	\$ 1,594,633
Investments	105,621,824	100,803,378
Dividends and interest receivable	-	17,455
Prepaid expenses and deposits	76,835	107,087
Property and equipment, net	<u>281,184</u>	<u>314,897</u>
Total Assets	\$ <u>107,395,324</u>	\$ <u>102,837,450</u>
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable and accrued liabilities	\$ 353,358	\$ 309,230
Grants payable	<u>2,099,317</u>	<u>2,561,137</u>
Total liabilities	<u>2,452,675</u>	<u>2,870,367</u>
Unrestricted Net Assets	<u>104,942,649</u>	<u>99,967,083</u>
Total Liabilities and Net Assets	\$ <u>107,395,324</u>	\$ <u>102,837,450</u>

The accompanying notes are an integral part of the financial statements

CONNECTICUT HEALTH FOUNDATION, INC.
STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Revenues		
Unrealized investment gains (losses)	\$ 6,982,668	\$ (8,437,879)
Realized investment gains	2,595,064	523,159
Interest and dividend income	1,712,269	2,631,339
Total revenues	<u>11,290,001</u>	<u>(5,283,381)</u>
Expenses		
Grants and program related expenses	4,431,999	4,887,914
General administrative expenses	1,173,552	1,093,499
Investment expenses	708,884	719,923
Total expenses	<u>6,314,435</u>	<u>6,701,336</u>
Increase (Decrease) in Net Assets	4,975,566	(11,984,717)
Net Assets - Beginning of Year	<u>99,967,083</u>	<u>111,951,800</u>
Net Assets - End of Year	<u>\$ 104,942,649</u>	<u>\$ 99,967,083</u>

The accompanying notes are an integral part of the financial statements

CONNECTICUT HEALTH FOUNDATION, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	2012	2011
Cash Flows from Operating Activities		
Change in net assets	\$ 4,975,566	\$ (11,984,717)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation	44,690	51,686
Unrealized (gain) loss on investments	(6,982,668)	8,437,879
Realized gain on investments	(2,595,064)	(523,159)
(Increase) decrease in operating assets:		
Dividends and interest receivable	17,455	25,074
Prepaid expenses and deposits	30,252	(51,080)
Increase (decrease) in operating liabilities:		
Accounts payable and accrued liabilities	44,128	(254,809)
Grants payable	(461,820)	(190,863)
Net cash used in operating activities	(4,927,461)	(4,489,989)
Cash Flows from Investing Activities		
Purchase of property and equipment	(10,977)	(29,993)
Purchases of investments	(72,147,953)	(166,101,696)
Proceeds from the sale of investments	76,907,239	171,668,200
Net cash provided by investing activities	4,748,309	5,536,511
Net Increase (Decrease) in Cash and Cash Equivalents	(179,152)	1,046,522
Cash and Cash Equivalents - Beginning of Year	1,594,633	548,111
Cash and Cash Equivalents - End of Year	\$ 1,415,481	\$ 1,594,633

The accompanying notes are an integral part of the financial statements

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Connecticut Health Foundation, Inc. (the Foundation) is a not-for-profit corporation organized under the laws of the State of Connecticut. The purpose of the Foundation is to promote the health and welfare of the people of Connecticut.

Basis of Accounting and Presentation - The Foundation prepares its financial statements on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP). Net assets, revenues and expenses are classified based on the existence or absence of donor-imposed restrictions. Under applicable accounting standards, the net assets of the Foundation are considered to be unrestricted.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Management has made estimates based on assumptions for the fair value of financial instruments, specifically alternative investments. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents - Cash equivalents are defined as highly liquid investments with original maturities of 90 days or less. The Foundation maintains deposits in financial institutions that may, at times, exceed federal depository insurance limits. Management believes it adequately mitigates this risk by only investing in major financial institutions. However, the Foundation has not experienced any losses in such accounts and management believes the Foundation is not exposed to any significant credit risk on cash and cash equivalents.

Investment Valuation and Income Recognition - Investments are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note 2 for a discussion of fair value measurements.

Purchases and sales of securities are recorded on the trade date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net realized and unrealized gains (losses) on investments include the Foundation's gains and losses on investments bought and sold as well as held during the year. Realized and unrealized gains and losses and investment income are classified as increases and decreases in unrestricted net assets.

The Foundation's investments in debt and equity securities are exposed to interest rate, market, credit and other risks depending on the nature of the specific investment. Accordingly, it is at least reasonably possible that these factors will result in changes in the value of the Foundation's investments, which could materially affect amounts reported in the financial statements.

Property and Equipment - Purchases of \$1,000 or more, whether individually or in the aggregate, are capitalized. Furniture, fixtures and equipment are stated at cost, less accumulated depreciation, and are depreciated using the straight-line method over the estimated useful lives of the assets, which range from 2-10 years. Leasehold improvements are stated at cost, less accumulated depreciation, and are depreciated using the straight-line method over the remaining term of the lease.

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Repairs and maintenance are charged to expense as incurred. Depreciation expense for the years ended December 31, 2012 and 2011 was \$44,690 and \$51,686, respectively.

Federal Excise Taxes - As an organization described in Section 501(c)(3) of the Internal Revenue Code, the Foundation is exempt from federal income taxes and has been classified as a private foundation. In accordance with the applicable provisions of the Internal Revenue Code, the Foundation is subject to an excise tax on net investment income, including realized gains, and to tax on unrelated business income in connection with certain partnership investments. Excise tax expense for the years ended December 31, 2012 and 2011, was \$62,038 and \$49,867, respectively.

The Foundation has provided for deferred income taxes at the excise tax rate of 2%. Deferred excise taxes relate to net unrealized investment gains that have been recognized in the financial statements but are deferred from taxable income until realized. Total deferred excise tax recorded for the year ended December 31, 2012 is \$140,000. The Foundation's informational returns for the years ended December 31, 2009 through 2012 are subject to examination by the Internal Revenue Service and the Attorney General of the State of Connecticut.

In accordance with private foundation regulations, qualified minimum distributions are required to be made by the Foundation on an annual basis. Qualified distributions for the fiscal years ended December 31, 2012 and 2011, were \$ 2,652,896 and \$3,001,401, respectively.

Spending Policy - The Foundation follows a spending policy based upon the total return concept, which emphasizes total investment return, consisting of investment income and realized and unrealized gains and losses. Under the spending policy, a distribution of investment return is not contingent on the total investment return in that year. The spending formula is designed specifically to stabilize annual spending levels and to preserve the real value of the fund portfolio over time. The Foundation's spending is capped at 5.4% of a twenty-quarter running average of total invested assets. Spending will be sufficient to ensure that the 5% minimum requirement established by the Internal Revenue Service is met.

Risks and Uncertainties - Investment securities are exposed to various risks, such as interest rate, market and credit risk. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risk in the near term could materially affect the amounts reported in the statement of financial position and the statement of activities.

Reclassifications - Certain amounts reported in prior periods have been reclassified in order to conform to the current year presentation.

Subsequent Events - In preparing these financial statements, management has evaluated subsequent events through April 10, 2013, which represents the date the financial statements were available to be issued.

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - FAIR VALUE

Generally accepted accounting principles establish a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Foundation has the ability to access. Liquidity of this level of investments is daily.

Level 2 - Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability. The liquidity of this level of investments ranges from more than daily through quarterly.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement. The liquidity of this level of investment ranges from more than quarterly to illiquid.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs. When, as a practical expedient, an investment is measured at fair value on the basis of net asset value, its classification as Level 2 or 3 will be impacted by the ability to redeem the investment at net asset value at the measurement date. If there is uncertainty or the inability to redeem an investment at net asset value in the near term subsequent to the measurement date, the investment is categorized as Level 3. Valuation for investments maintained by fund managers or limited partnerships are based upon the most recent estimates determined by the fund managers or general partners after review by the Foundation's management. Adjustments to such values have been considered but none have been made.

The following is a description of the valuation methodologies used for assets measured at fair value:

Mutual Fund Equities - Equities are valued at the closing price reported in the active market in which the individual securities are traded.

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - FAIR VALUE (Continued)

Domestic Equity - Domestic equity is valued at the closing price reported in the active market in which the individual securities are traded. This investment class seeks to outperform equity market indices on a risk-adjusted basis. The redemption period for these investments ranges from daily to quarterly. There are no unfunded commitments related to this investment class.

International Equity - International equity is valued at the closing price reported in the active market in which the individual securities are traded. This investment class seeks to outperform the non-US equity market indices on a risk-adjusted basis. The redemption period for these investments ranges from daily to monthly, with 0-10 days notice. There are no unfunded commitments related to this investment class.

Fixed Income - Fixed income is valued at the closing price reported in the active market in which the individual securities are traded. This investment class invests in US treasuries, securities and diversified fixed income strategies, which invest in corporate credits, including bank loans, high yield and investment grade bonds. The redemption period for these investments ranges from daily to quarterly, with 0-60 days notice. There are no unfunded commitments related to this investment class.

Commodities - Interests in commodities are valued using net asset values as determined by the investment manager of the fund. This net asset value is based on the fair value of the underlying assets and liabilities of the related fund at the measurement date. This investment class seeks capital appreciation by investing in a portfolio of commodities within six groups (Agriculture, Base Metals, Precious Metals, Softs and Others, Energy and Livestock). The redemption period for these investments is monthly, with five days notice. There are no unfunded commitments related to this investment class.

Hedge Fund of Funds - Interests in hedge fund of funds are valued using net asset values as determined by the investment manager of the fund. This net asset value is based on the fair value of the underlying assets and liabilities of the related fund at the measurement date. This investment class seeks long-term equity like returns with minimal correlation to the major market average. There are no unfunded commitments related to this investment class.

Natural Resources - Interests in natural resources are valued using net asset values as determined by the investment manager of the fund. This investment class invests in a diversified portfolio of global natural resource and commodity securities. The fund does not have a specific return or volatility target, but rather focuses on generating absolute returns in all markets. The redemption period for these investments is quarterly, with 60 days notice. There are no unfunded commitments related to this investment class.

Real Estate - Interests in real estate are valued using net asset values as determined by the investment manager of the fund. This investment class makes commitments to private real estate investment opportunities with the goal of outperforming market indices over the long term. There are no unfunded commitments related to this investment class.

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - FAIR VALUE (Continued)

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Foundation believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following tables set forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of December 31, 2012 and 2011:

<u>Description</u>	<u>Fair Value Measurements Using</u>			
	<u>December 31,</u> <u>2012</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Mutual funds:				
Equity	\$ 1,726,597	\$ -	\$ 1,726,597	\$ -
Domestic equity:				
Large cap equity	18,073,857	10,250,963	7,822,894	-
Small cap equity	1,671,165	1,671,165	-	-
International equity:				
Developed	16,478,637	5,398,240	11,080,397	-
Emerging	10,266,516	10,266,516	-	-
Fixed income:				
Domestic governmental bonds	2,909,666	2,909,666	-	-
U.S. bonds	8,920,840	8,920,840	-	-
Global gov't nominal bonds	4,842,134	-	4,842,134	-
Emerging market debt	5,382,984	5,382,984	-	-
Marketable alternatives:				
Commodities	3,572,014	-	3,572,014	-
Hedge fund of funds	21,451,238	-	7,608,908	13,842,330
Natural resources	6,276,421	-	6,276,421	-
Nonmarketable alternatives:				
Real estate	1,721,783	-	1,721,783	-
Total investments	<u>103,293,852</u>	<u>44,800,374</u>	<u>44,651,148</u>	<u>13,842,330</u>
Cash held by portfolio manager	<u>2,327,972</u>	<u>2,327,972</u>	<u>-</u>	<u>-</u>
Total Assets at Fair Value	\$ <u>105,621,824</u>	\$ <u>47,128,346</u>	\$ <u>44,651,148</u>	\$ <u>13,842,330</u>

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - FAIR VALUE (Continued)

<u>Description</u>	<u>Fair Value Measurements Using</u>			
	<u>December 31, 2011</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Domestic equity:				
Large cap equity	\$ 18,751,604	\$ 18,751,604	\$ -	\$ -
Small cap equity	1,472,732	-	1,472,732	-
International equity:				
Developed	11,909,518	3,074,292	8,835,226	-
Emerging	9,107,757	9,107,757	-	-
Fixed income:				
Domestic governmental bonds	3,006,493	3,006,493	-	-
U.S. bonds	9,392,714	9,392,714	-	-
Global gov't nominal bonds	3,950,947	-	3,950,947	-
Emerging market debt	4,456,822	4,456,822	-	-
Marketable alternatives:				
Commodities	4,937,916	-	4,937,916	-
Hedge fund of funds	20,231,977	-	7,896,173	12,335,804
Natural resources	5,250,253	-	5,250,253	-
Nonmarketable alternatives:				
Real estate	1,486,185	1,486,185	-	-
Total investments	<u>93,954,918</u>	<u>49,275,867</u>	<u>32,343,247</u>	<u>12,335,804</u>
Cash held by portfolio managers included in cash and cash equivalents	<u>6,848,460</u>	<u>6,848,460</u>	<u>-</u>	<u>-</u>
Total Assets at Fair Value	\$ <u>100,803,378</u>	\$ <u>56,124,327</u>	\$ <u>32,343,247</u>	\$ <u>12,335,804</u>

During the year ended December 31, 2012, there were transfers from Level 3 to Level 2 of \$5,249,964. There were no transfers for the year ended December 31, 2011.

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - FAIR VALUE (continued)

Additional information regarding investments that report fair value based on net asset value per share or unit as of December 31, 2012 is as follows:

<u>Description</u>	<u>Fair Value</u>	<u>Redemption Terms</u>	<u>Redemption Restrictions</u>
Domestic equity - large cap	\$ 7,822,894	Daily to Quarterly	-
International equity - developed	11,080,397	Daily to Monthly	10 days written notice
Fixed income - global bond fund	4,842,134	Monthly	-
Commodities	3,572,014	Monthly	-
Hedge fund of funds	17,837,963	Monthly to Annually with lock up periods of one to two years	0 to 90 days written notice
Real estate	1,721,783	Monthly	-
Natural resources	<u>6,276,421</u>	Daily	-
Total	\$ <u>53,153,606</u>		

There were no unfunded commitments for the year ended December 31, 2012.

The investment strategies of the portfolio maintained by the Foundation are as follows:

- (a) The investment objective is to provide a reliable source of funds to support the Foundation's spending needs, which include grantmaking, program related initiatives and operations and administrative expenses, while achieving an investment return sufficient to maintain or grow the funds' purchasing power in perpetuity.
- (b) The performance object is to achieve a real total annualized return greater than the combined total of the spending policy and investment expenses, on average, over a typical market cycle (generally considered to be five years). The target of real return, net of all investment expenses, is 5% over any rolling five-year period.
- (c) The fund will be invested in a manner that is expected to preserve its purchasing power in real terms after spending and maximize its long term total return with reasonable and acceptable levels of investment risk. Investment risk is defined in two ways: (i) the possibility of the investments decline in value and (ii) the expected performance volatility of the investments in the portfolio. The portfolio will comprise investments made in multiple asset categories in order to safeguard the portfolio's capital and to lower overall portfolio risk.

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 2 - FAIR VALUE (continued)

The table below sets forth a summary of changes in the fair value of the Foundation's Level 3 assets for the years ended December 31, 2012 and 2011:

		<u>Marketable Alternatives - Hedge Fund of Funds</u>
Balance - January 1, 2011	\$	608,175
Total losses (realized and unrealized) included in the change in net assets		(522,335)
Sales		-
Purchases		12,249,964
Transfers		<u>-</u>
Balance - December 31, 2011		12,335,804
Total gains (realized and unrealized) included in the change in net assets		556,490
Sales		-
Purchases		6,200,000
Transfers to Level 2		<u>(5,249,964)</u>
Balance - December 31, 2012	\$	<u><u>13,842,330</u></u>

The Board of Directors approves the overall investment strategy and guidelines of the Foundation, which are implemented with full discretion by the external Chief Investment Officer. Management fees for investment managers and advisors were approximately \$708,884 and \$719,923 for the years ended December 31, 2012 and 2011, respectively.

NOTE 3 - GRANTS PAYABLE

Grants authorized but unpaid at year-end are reported as liabilities. The following is a summary of grants authorized and payable at December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
To be paid in 2012	\$ -	\$ 2,371,137
To be paid in 2013	1,874,317	190,000
To be paid in 2014	<u>225,000</u>	<u>-</u>
Total	<u>\$ 2,099,317</u>	<u>\$ 2,561,137</u>

CONNECTICUT HEALTH FOUNDATION, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 4 - RETIREMENT PLANS

The Foundation sponsors a safe-harbor 401(k) and a Roth 401(k) plan for its employees. The election period for new participants is generally 60 days before their one-year anniversary date. The employer will match dollar for dollar up to 3% of the employee's eligible compensation and fifty cents per dollar for contributions of 4% and 5%. These dollars are 100% vested at the time they are paid. For the years ended December 31, 2012 and 2011, total cost to the Foundation was \$31,828 and \$27,367, respectively.

NOTE 5 - OPERATING LEASES

The Foundation leases office space in Hartford, Connecticut, under an operating lease that expires August 2021. The lease requires escalating monthly payments ranging from \$10,328 to \$10,872 over the term of the lease. The Foundation recognizes rent expensed on a straight-line basis over the respective lease term of the underlying agreement. Rent expense under this method was \$117,396 and \$117,407 for the years ended December 31, 2012 and 2011, respectively.

The Foundation entered into a lease agreement in February 2012 to lease a copier under a noncancelable operating lease with a term of more than one year. Rental expense amounted to \$5,972 for the year ended December 31, 2012.

The following is a schedule of future minimum payments required under the above leases as of December 31, 2012.

2013	\$	131,899
2014		131,899
2015		131,899
2016		134,617
2017		132,451
Thereafter		<u>467,482</u>
	\$	<u><u>1,130,247</u></u>