2017 ANNUAL REPORT

Opportunity.

We see each achievement as a new challenge to prove ourselves.

SEE OUR PROGRESS →

A MESSAGE FROM JOE

The scope of working to protect the health, security and independence of millions of Americans is epic. Yet, grand opportunity is born from incremental achievement.

Never has this been more evident than in 2017, when Palmetto GBA was awarded the Jurisdiction J (JJ) A/B MAC contract. A historical moment for us – granting us more than 15 percent of the Medicare A/B market share – it provides us with the chance to set a new standard of excellence for MAC implementations. Similar to achieving 99.7 percent across all contract performance metrics or delivering an initial seven-month program savings exceeding $63 million last year on the Home Health Pre-Claim Review demonstration project, this team knows what it means to deliver on its promise.

As we step up to the plate and into tomorrow, we will continue to seek ways to elevate the integrity of each healthcare transaction we touch, every day. We'll ensure individual snapshot moments of customer interactions matter. We're bringing our best to the table, and we're ready.

Best Regards,

WALTER J. JOHNSON
President & COO

OUR PHILOSOPHY

We believe technical and administrative solutions have the power to enhance service and quality. And we are constantly striving to reach new heights of performance to improve the quality of life for our customers, employees and communities.

PALMETTO GBA®
A CELERIAN GROUP COMPANY

Palmetto GBA is a leading provider of high-volume claims and transaction processing, contact center operations and technology services to the federal government. Our core business is to provide support to the Centers for Medicare & Medicaid Services (CMS), Medicare beneficiaries and Medicare providers.

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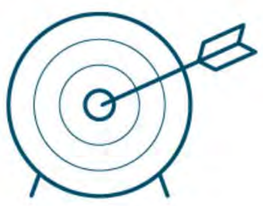
PROGRESS

Non-negotiable standards that uphold true performance

Crystal-clear purpose. Laser-sharp focus on process improvement. And the technical savvy to refine innovation. We believe the compounding effect of these drives progress. Demonstrated every day by our associates, in large and small ways, these moments propel exceptional achievement and the opportunity to continually improve ourselves. Read about it in our four areas of performance.



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PROGRESS | METRICS

Unparalled performance

Palmetto GBA's performance across all contract metrics in 2017 was 99.7 percent, achieving 100 percent performance in six months.

99.7%
metrics met

2017 SCALE

$42.8 bil
Benefits Paid

114 mil
Claims Processed

7.6 mil
Beneficiaries Served

1.6 mil
Inquiries Answered

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PROGRESS | IMPACT

Stepping up to the plate

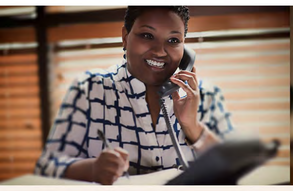
JURISDICTION J AWARD IS AN INCREDIBLE HONOR

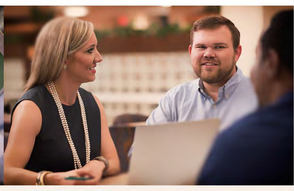
September 2017 brought a historic win for Palmetto GBA.

Following a more than yearlong competitive bidding process, the Centers for Medicare & Medicaid Services (CMS) selected Palmetto GBA as the Medicare Administrative Contractor for Jurisdiction J, which includes the states of Alabama, Georgia and Tennessee. Jurisdiction J represents 6.9 percent of the national Part A/Part B claim-volume workload.

The five-year contract will employ more than 460 administrative and professional employees within Palmetto GBA offices in Alabama and South Carolina. Work includes provider enrollment, outreach and education, Medicare claims processing, appeals, provider customer service, medical review, and audit and reimbursement. According to CMS, Jurisdiction J includes more than 2.5 million Medicare beneficiaries, more than 52,000 physicians and 400 hospitals that serve Medicare patients.

CMS has stringent standards for contract performance and measures execution through a variety of processes, including on-site oversight, data reviews and protocol-driven quality assurance reviews, and independent audits. Our years of delivering innovative solutions for CMS position us well to exceed their expectations and provide countless opportunities for the Palmetto GBA team to grow to new heights.





2017 BEST PRACTICE RECOGNITION FOR ETHICS & COMPLIANCE

Last year, Palmetto GBA was recognized with a **2017 Best Practice Award** by the Health Ethics Trust for *Integrating Audit and Internal Controls with Ethics and Compliance*. We're proud of the acknowledgement recognizing what our internal team already knows: Palmetto GBA's ongoing compliance program efforts support strong internal controls.

Health Ethics Trust is a division of the Council of Ethical Organizations and works to assist healthcare organizations committed to ethical and legal conduct in coping with compliance requirements. Best practice award criteria include demonstration of:

- Established policies and procedures
- Detailed documentary evidence of segregation of duties
- Ongoing associate training
- Checks and internal verification within business units
- Conduct risk assessments for the entire organization

Congratulations to the entire Palmetto GBA team, especially the Internal Audit Department that works diligently with the Compliance Unit to ensure compliance with applicable laws and regulations and to safeguard the effectiveness of our internal controls.

MEDICARE INTEGRITY PROGRAM

Our program safeguard activities resulted in significant savings for Medicare.

HOVER OVER ACRONYMS TO REVEAL FULL NAMES	JM A/B MAC	RRB
BI	n/a	$1,345,749
MSP	$539,574,452	$5,812,293
MR	$632,935,814	$9,918,915
MR Ambulance Prior Auth	$12,659,670	n/a
Total	$1,185,169,936	$17,076,957

$1.2 bil
2017 Medicare Program Savings

REQUEST FOR ADVANCE PAYMENT SUPPRESSION PROCESS

Palmetto GBA's innovative Request for Advance Payment (RAP) suppression process continues to produce savings for the Medicare Program. In 2017, this improvement created suppression of more than 21,000 RAPs for which final claims were never submitted. Using an average RAP of $771, the RAP suppression process resulted in $16.2 million in savings for the Medicare program.

$16.2 mil
2017 savings

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PROGRESS | GROWTH

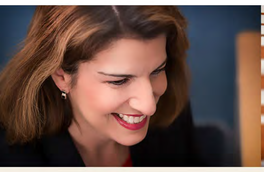
Perpetual advancement

GROWTH INITIATIVE

In 2017, Palmetto GBA continued developing the expertise and infrastructure to provide data analytics services and technology to targeted federal agencies. This strategic initiative will enhance our IT offerings, diversify customers and broaden federal government contract vehicle access. We can then offer even more comprehensive technology and business management services to both the public and private sectors.

Last year, we developed and executed an acquisition strategy that has resulted in growth for our company. We refined and focused the initiative's strategic direction, as well as continued to build our team of talented professionals. The initiative's ongoing objectives include:

- Obtain additional contract vehicles
- Align with companies that have outstanding performance and growth potential
- Build capabilities and synergies



NEW BUSINESS

STRATEGIC PARTNER ACQUISITION OF RESOURCES CONTRACT (SPARC)

SPARC is a multiple-award, Indefinite Delivery/Indefinite Quantity (IDIQ), performance-based contract available to all components within CMS and all Health and Human Services Operating Divisions. Through it, partners procure IT System development services, from end to end. Its purpose is to provide strategic, technical, and program management guidance and support services, and to facilitate the modernization of CMS business processes and supporting systems and their operations.

Palmetto GBA participated on several SPARC teams, and as a sub-contractor our teams were awarded four SPARC contracts — one full and open unrestricted seat and three reserved for small business participation.

JURISDICTION J A/B MAC

Palmetto GBA was awarded the Jurisdiction J A/B MAC contract. Under this contract Palmetto GBA will perform all the Medicare Parts A and B administration for the jurisdiction, including provider enrollment, outreach and education, Medicare claims processing, appeals, provider customer service, medical review, and audit and reimbursement. This jurisdiction includes the states of Alabama, Georgia and Tennessee, and represents 6.9 percent of the national Part A/Part B claim-volume workload. Read more

RENEWED CONTRACTS

Year after year Palmetto GBA is rehired to continue delivering innovations and efficiencies for its contract clients. As a sought-after partner by the federal government, we are proud of every renewed contract and see each as an opportunity to better ourselves. Each win is a huge accomplishment. We're proud of them all.

CONTINUING EDUCATION (CE) SUPPORT & MEDICARE LEARNING NETWORK (MLN) PRODUCT DEVELOPMENT

Retaining the contract since 2002, Palmetto GBA again was awarded the CE-MLN Contract formerly known as the Provider Education and Support Services Contract. The contract supports and develops Medicare educational materials for healthcare professionals.

In 2017, Palmetto GBA's CE-MLN contract:

- Produced 97 web-based training courses for the Medicare Learning Network™, including content development, programming, testing and 508 compliance
- Produced 89 provider education publications for the Medicare Learning Network™, including fact sheets, booklets and education tools
- Processed, maintained and reported on evaluation, post-activity survey, and certificate data for 136,948 participants
- Wrote and designed two successful reaccreditation application portfolios for:
    - the Accreditation for Continuing Medical Education's (ACCME) prestigious Accreditation with Commendation
    - the International Association for Continuing Education and Training (IACET) Authorized Provider status
- Facilitated the Centers for Medicare and Medicaid Services Continuing Education's (CMSCE) national leadership role in the Alliance for Continuing Education in the Healthcare Professions Federal Educators (ACEHP) member section

THIRD PARTY LIABILITY (TPL) WITH SC MEDICAID

As a subcontractor to the Celerian Group Medicaid division, Palmetto GBA again was awarded the Third-Party Liability contract in August 2017. Its purpose is to provide financial and IT services in support of the Medicaid Third Party Liability (TPL) for South Carolina. Successfully rehired for this work since May 2011, Palmetto GBA has traditionally handled the disposition of all solicited Medicaid TPL checks received, including initiating debit and credit adjustments. Additionally, Palmetto GBA administers the Health Insurance Premium Program and processes quarterly credit balance reports submitted by institutional providers. When the new contract begins later in 2018, Palmetto GBA will continue to maintain all previous responsibilities and assume added case management responsibilities for casualty, estate recovery, class action suits, and special needs trusts.

FRONT-END SYSTEM (FES)

For nearly 20 years, Palmetto GBA has successfully retained the Front-End System (FES) contract (previously the CSFES). The contract's purpose is to collect and process all Medicare Part C and Part D program data records around the clock. As the FES contractor, Palmetto GBA is responsible for the design, development, testing, implementation, operation, and maintenance of these four front-end systems.

In 2017, the national contract processed more than 3.8 billion encounter claims, risk adjustment transactions, prescription drug events and Medicare/Medicaid dual eligible claims, serving 728 Medicare Advantage plans with more than 44 million enrolled beneficiaries.

WEST VIRGINIA MEDICAID AUDIT

Palmetto GBA once again was awarded the contract for the West Virginia Medicaid Audit to provide cost report desk review, field audit, and other necessary services to assist the West Virginia Department of Health and Human Resources, Office of Accountability and Management Reporting, in meeting its Title V (Maternal and Child Health) and Title XIX (Medicaid) cost report settlement requirements. This is done in conjunction with the provider's annual Title XVIII (Medicare) cost report settlement, if applicable.

As needed, Palmetto GBA performs additional tasks for the department to analyze its provider payment methodologies, or other necessary tasks for the efficient operation and management of its Title V and Title XIX Programs.

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PROGRESS | INNOVATIONS

Constant evolution

REFINED INNOVATIONS

Suite of eServices

Palmetto GBA continues to expand tools on our industry leading provider portal to include trend reporting, multiple provider comparative reports, and other devices to assist groups and individual providers with their Medicare business analytics. We're now leveraging this suite of products and their use by providers to develop our Provider Behavior Analytics Engine (PBAE). PBAE goes beyond the typical outlier analytics and uses their interaction with these new analytic tools to allow a provider to either self-correct or self-select themselves for additional interventions. Our portal efforts remain highly visible with our customers, and we work closely with them to define new requirements and look for additional features to develop.

PALMETTO GBA®
eServices

Debt Management System (DMS)

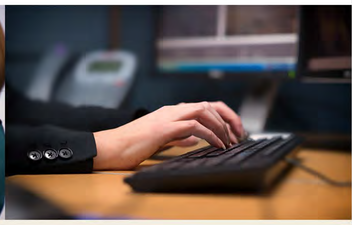
Palmetto GBA seeks to modernize Medicare debt management activities. In 2017, DMS improved automated data entry processes, augmented system response and enhanced error handling. These modifications resulted in heightened system productivity and more efficient handling of processing errors. In addition, system-wide flags were implemented to better integrate activities between operational areas and improve visibility of high-priority actions.

iDA (Intelligent Document Automation) Project

Palmetto GBA is further developing our ability to receive and process both the electronic and automated clinical data we receive from the provider community in support of medical review documentation requests, appeals and prior authorization. iDA includes the tools to facilitate automated adjudication.

iDA also includes implementation of Natural Language Processing (NLP) and Artificial Intelligence (AI) to assist a reviewer in making the clinical decision. While we do not expect to fully rely on NLP/AI engines to make clinical decisions, our goal simply is to become more effective reviewers. We're currently reviewing and piloting several AI-based products supporting clinical decision making. These pilot projects, performed in conjunction with CMS's Center for Program Integrity, are integral as we experiment and conduct research/development for the following solutions:

- **C.A.R.D. (Computer Assisted Review Decision)** – uses AI based on Acceptable Use Criteria to provide immediate review and scoring of a home health Electronic Medical Record (EMR) to assist Medical Review in identification of claims with potential errors
- **iMarker** – identifies and organizes critical text and required information for review



ENHANCED SECURITY SYSTEMS

The Centers for Medicare & Medicaid Services (CMS) has increased its focus on systems security and heightened its number of security requirements, including a 20 percent increase in controls to be implemented by September 25, 2018. To meet — and exceed — these expectations, Palmetto GBA remains committed to improved overall system security.

In the last year, Palmetto GBA made more than 15 enhancements to the Security Manager Application, including the ability to process the new JJ A/B MAC information. Continued automation has reduced audit issues, errors and costs associated with the controls, and we are planning further developments in 2018.

The IP-360 system security score provides CMS with a viable and base metric for measuring IT risk on our Medicare network. Maintaining an "A" is a strong indicator that Palmetto GBA's patch and configuration management programs are working well, even considering the major challenges presented by Meltdown and Spectre.

IP-360 System Security maintained an "A" rating for the past **51 consecutive months.**

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PHILANTHROPY

A way of life

"The integrity and deep commitment to improving lives I see in each Palmetto GBA associate is humbling. Day in and day out, your care for each other, the communities in which we live, and the many social and public health issues we touch inspires awe. Your kindness and generosity are the fabric of who we are and are fundamental to our every success. I am proud to walk this journey with you."

— WALTER J. JOHNSON, President & COO

In 2017, the Palmetto GBA team collectively made a difference to more than 30 organizations. We met a variety of needs by collecting items for the homeless, volunteering our time and donating our resources to organizations and events like American Heart Association, Palmetto Place Children's Shelter, United Way and American Cancer Society's Relay for Life.

32
organizations reached by Palmetto GBA team members

26
families adopted through Families Helping Families

$288,612
donated to United Way

$11,000
donated to local organizations where we work and live

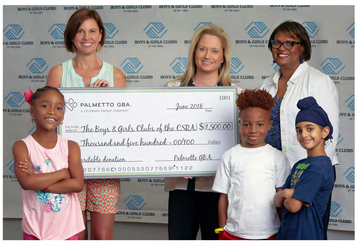
2,962
meals and 3,770 bottles of water provided to nourish those in need

2,000
school supplies donated to children's organizations and schools

2017 BEST OF PHILANTHROPY AWARDS

To honor and recognize associates' admirable commitment to community service, Palmetto GBA developed two awards — Gifts of Time & Talent and Gifts of Treasure — allowing winners to grant $3,000 to the charities of their choice.

The 2017 Best of Philanthropy Award Gifts of Time & Talent winner is the Augusta Operations' Relay for Life Team. This team shared their time volunteering throughout a 24-hour American Cancer Society fundraising event. They also used their baking and food sale talents to raise money for the organization. The team also chose to help local children by donating their grant money to The Boys and Girls Club of Augusta.



The 2017 Best of Philanthropy Award Gift of Treasure winner is Support Services' Foster Care Bay Drive. This division collected duffel bags, backpacks and small suitcases for foster care children who otherwise travel from foster home to foster home with their belongings in a paper grocery bag. Continuing their support of children they divided their grant money between Palmetto Place Children's Shelter in Columbia and Sacks of Love in Kershaw County.

AWARD CRITERIA

- Understanding community needs
- Creativity in meeting community needs
- Community collaboration
- Participation/ Collaboration
- Volunteer Engagement
- Ongoing Support

LEADERSHIP

Board of Directors

David Pankau
CHAIRMAN, BOARD OF DIRECTORS

Palmetto GBA, LLC

PRESIDENT & CEO

BlueCross BlueShield of South Carolina

M. Edward Sellers
CHAIRMAN, BOARD OF DIRECTORS

BlueCross BlueShield of South Carolina

Joseph Sullivan
CHAIRMAN EMERITUS, BOARD OF DIRECTORS

BlueCross BlueShield of South Carolina

Bruce W. Hughes
PRESIDENT & COO

Celerian Group, BlueCross BlueShield of South Carolina

Joe Johnson
PRESIDENT & COO

Palmetto GBA, LLC

Brian Rubin
RETIRED

Department of Defense TRICARE Management Activity

Martin Kappert
RETIRED DEPUTY ASSISTANT SECRETARY

Health Affairs, Department of Defense

Ilene H. Nagel
MANAGING DIRECTOR

Russell Reynolds Associates

David Butler
RETIRED COO

Strategic Management Systems, Inc.

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PRESIDENT & COO

Mike Barlow
VICE PRESIDENT

Jurisdiction J A/B MAC Operations

Nella Bishop
CIO & VICE PRESIDENT

Systems & Support

Neal Burkhead
VICE PRESIDENT

Shared Services

Robin Free
ASSISTANT VICE PRESIDENT

Pre-Claim Review

Elaine Garrick
VICE PRESIDENT

Support Operations

Ken Lewis
VICE PRESIDENT & CFO

Tim Masheck
VICE PRESIDENT

Information Technology Services

Lee McElveen
VICE PRESIDENT

Compliance & Privacy

Margaret Price
VICE PRESIDENT & CTO

Ed Sanchez
VICE PRESIDENT

Jurisdiction M A/B MAC Operations

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2017

Financial Report

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03 Statements of Comprehensive Income
03 Statements of Changes in Member's Equity
04 Statements of Cash Flows
05 Notes to Financials Statements

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Opportunity.

INDEPENDENT AUDITOR'S REPORT

BOARD OF DIRECTORS
PALMETTO GBA, LLC

MAULDIN & JENKINS

Report on the Financial Statements

We have audited the accompanying financial statements of Palmetto GBA, LLC which comprise the balance sheet as of December 31, 2017, and the related statements of operations, comprehensive income, changes in member's equity, and cash flows for the year then ended, and the related notes to the financial 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.

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 of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a reasonable 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 Palmetto GBA, LLC at December 31, 2017, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States.

Other Matter

The financial statements of Palmetto GBA, LLC, as of and for the year ended December 31, 2016, were audited by Derrick, Stubbs and Stith, LLP (predecessor auditors), whose partners joined Mauldin & Jenkins, LLC on October 1, 2017. Derrick, Stubbs and Stith, LLP's report dated March 2, 2017, expressed an unmodified opinion on those statements.

Mauldin & Jenkins, LLC

Columbia, South Carolina
March 9, 2018

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BALANCE SHEETS (IN THOUSANDS)

	December 31, 2017	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ 43,682	$ 37,827
Restricted Medicare Funds	4,320	3,649
Accounts receivable	26,864	29,509
Accounts receivable from affiliates	1,568	1,107
Accrued revenue	39,710	44,819
Prepaid expenses	385	685
Deferred income taxes	1,880	3,412
Total current assets	118,409	121,008
Long-term assets:		
Equipment and Leasehold Improvements, net of accumulated depreciation of $31,242 and $30,842 in 2017 and 2016, respectively	3,405	3,627
Investments – available for sale	15,091	5,077
Investments – held-to maturity	24,085	23,456
Investments in affiliates	524	1,871
Deferred income taxes	4	35
Total long-term assets	43,109	34,066
Total assets	**$ 161,518**	**$ 155,074**
LIABILITIES AND MEMBER'S EQUITY		
Current liabilities:		
Accrued payroll, taxes and benefits	$ 17,236	$ 15,942
Payable to parent	7,219	9,023
Restricted Medicare Funds	4,320	3,649
Other liabilities	10,036	12,318
Deferred income taxes	69	46
Total current liabilities	38,880	40,978
Long-term liabilities:		
Deferred income taxes	649	1,127
Total long-term liabilities	649	1,127
Member's equity:		
Contributed capital	34,961	34,961
Retained earnings	87,040	78,073
Accumulated other comprehensive income (loss)	(12)	(65)
Total member's equity	121,989	112,969
Total liabilities and member's equity	**$ 161,518**	**$ 155,074**

PALMETTO GBA, LLC (a single-member, limited liability company owned by BlueCross BlueShield of South Carolina)

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

STATEMENTS OF OPERATIONS (IN THOUSANDS)

	Years ended December 31, 2017	2016
REVENUES		
Railroad Retirement Board	$ 18,540	$ 18,225
JJ AB MAC	1,351	–
JM AB MAC	120,691	118,371
Other revenues	80,852	79,167
Total revenues	221,434	215,763
EXPENSES		
General and administrative expenses	206,458	203,251
Other expenses	180	180
Total expenses	206,638	203,431
Operating income	14,796	12,332
OTHER INCOME		
Investment income	336	932
Total other income	336	932
Income before income taxes	15,132	13,264
Provision for income taxes	6,165	4,615
Net Income	**$ 8,967**	**$ 8,649**

STATEMENTS OF COMPREHENSIVE INCOME (IN THOUSANDS)

	Years ended December 31, 2017	2016
Net income	**$ 8,967**	**$ 8,649**
Other comprehensive income (loss)		
Unrealized gain(loss) on investments:		
Unrealized holding gains arising during period, net of income tax (benefit) of ($7) and ($11) in 2017 and 2016	(12)	(20)
Less: reclassification adjustment for OCI included in net income, net of income tax expense of $35 and $7 in 2017 and 2016	65	12
Total unrealized gain(loss) on investments	53	(8)
Comprehensive income	**$ 9,020**	**$ 8,641**

STATEMENTS OF CHANGES IN MEMBER'S EQUITY (IN THOUSANDS)

	Contributed Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance January 1, 2016	$ 34,961	$ 69,424	$ (57)	$ 104,328
Net income	–	8,649	–	8,649
Other comprehensive (loss)	–	–	(8)	(8)
Balance December 31, 2016	34,961	78,073	(65)	112,969
Net income	–	8,967	–	8,967
Other comprehensive	–	–	53	53
Balance December 31, 2017	**$ 34,961**	**$ 87,040**	**$ (12)**	**$ 121,989**

PALMETTO GBA, LLC (a single-member, limited liability company owned by BlueCross BlueShield of South Carolina)

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

STATEMENTS OF CASH FLOWS (IN THOUSANDS)

	Years ended December 31, 2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 8,967	$ 8,649
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	425	531
Amortization on bonds	620	107
Loss on equipment and leasehold improvements disposals	4	15
Realized loss(gain) on investments	49	(149)
Unrealized (gain)loss on investments	(80)	12
Change in other comprehensive gain/(loss)	53	(8)
Equity in income of affiliates	1,347	(40)
Deferred income tax provision	1,108	(710)
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable and accrued revenue	7,754	(4,780)
(Increase) decrease in receivables from affiliates	(461)	551
Decrease in prepaid expense	300	1
Increase in accrued payroll, taxes and benefits	1,294	2,453
(Decrease) increase in payable to parent	(1,804)	1,563
(Decrease) in other liabilities	(2,282)	(644)
Net cash provided by operating activities	17,294	7,551
CASH FLOWS FROM INVESTING ACTIVITIES		
Equipment and leasehold improvements purchased	(207)	(379)
Investments redeemed — held-to-maturity	4,348	2,685
Investments sold — available-for-sale	5,085	5,681
Investments purchased — held-to-maturity	(5,547)	(22,232)
Investments purchased — available-for-sale	(15,118)	(1,557)
Net cash (used in) investing activities	(11,439)	(15,802)
Net increase/(decrease) in cash and cash equivalents	5,855	(8,251)
Cash and cash equivalents beginning of year	37,827	46,078
Cash and cash equivalents end of year	**$ 43,682**	**$ 37,827**
Supplemental disclosures of cash paid during the year for:		
Income taxes	$ 6,352	$ 6,124

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NOTE 1

BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Palmetto GBA, LLC (the Company) is a single-member limited liability company organized on January 1, 1998. The Company's sole member is Blue Cross and Blue Shield of South Carolina (BCBSSC). The Company is engaged in the business of providing Medicare Administrative Contractor (MAC) and Specialty Medicare Administrative Contractor (SMAC) services in various states. These services include health insurance claims processing and payment, customer service for health care providers, and payment safeguard functions designed to detect and prevent fraud and abuse in the Medicare program. The Company provides services to Medicare beneficiaries residing in various states and territories. The Company's major customer is the Centers for Medicare and Medicaid Services (CMS), the federal agency with fiduciary responsibility for the Medicare program.

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of 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.

Significant accounting policies and the methods of applying those policies are summarized below:

Cash, cash equivalents and credit risk

Restricted cash and the related restricted cash liability includes funds held for processing Medicare benefits paid to providers and beneficiaries of $4,320,000 and $3,649,000 at December 31, 2017 and 2016, respectively.

Cash equivalents represent certificates of deposit that have maturities of less than three months at date of purchase and money market fund investments. Market risk for cash and cash equivalents is limited to any one institution when deposits exceed federally insured limits. The Company had cash deposits in excess of federally insured limits in the approximate amount of $46,873,000 and $40,538,000 at December 31, 2017 and 2016, respectively. The Company has not experienced any losses on these accounts and management considers this to be a normal risk.

Financial instruments

The Company holds certain financial instruments including cash and accounts receivable. Management believes that the carrying values of financial instruments approximate fair value as required by Financial Accounting Standards Board (FASB) rules.

Subsequent events

Subsequent events have been evaluated through March 9, 2018, which is the date the financial statements were available to be issued. No events have occurred through that date that would require recognition or disclosure in the financial statements.

Equipment and leasehold improvements

Equipment and leasehold improvements are stated at amortized cost. Depreciation on new assets purchased is computed using the straight-line method over the estimated useful lives of the respective assets: four to eight years for furniture and fixtures, three to five years for data processing equipment and software, and four years for automobiles. Leasehold improvements are depreciated over the lesser of the remaining lease term or estimated useful life of the asset. Depreciation on used assets purchased is computed by using the straight-line method over the estimated remaining useful lives at the time of purchase of the respective assets.

Investment in affiliates

The Company has a 25% interest in TriCenturion, Inc. that is accounted for using the equity method. The Company's proportionate share of earnings or losses of this affiliate are reflected in income as earned and dividends or distributions are credited against investment in affiliate when received. The Company has not received any dividends as of December 31, 2017 and 2016.

Assets, liabilities and results of operations for TriCenturion, Inc. were as follows (in thousands):

	Years ended December 31,	
	2017	2016
Assets	$ 7,489	$ 14,069
Liabilities	$ 5,406	$ 6,561
Net Income	$ (425)	$ 218

Investments

Investments are comprised of common stocks, mutual funds, bonds, and United States Government mortgage-backed securities. These assets are accounted for in accordance with FASB guidance which requires that fixed maturities are to be classified as either "held to maturity", "available for sale", or "trading".

Management determines the appropriate classification of its fixed maturity securities at the time of purchase and reevaluates such designation as of each balance sheet date. Fixed maturity securities are classified as held to maturity as the Company has the positive intent and ability to hold them to maturity. Held-to-maturity securities are stated at amortized cost, adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization as well as interest earned is included in investment income.

Fixed maturity and equity securities not classified as held-to-maturity are classified as available for sale. Available-for-sale securities are carried at fair value based on published prices, with the unrealized gains and losses reported in member's equity. The amortized cost of debt securities in this category is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and interest earned is included in investment income. The cost of securities sold is based on the specific identification method.

Revenue recognition policies

The Company recognizes revenue on the Jurisdiction M A/B MAC, Data Computer Corporation of America (DCCA), National Supplier Clearinghouse (NSC) MAC, Railroad Retirement Board SMAC, and Jurisdiction J A/B MAC contracts on cost plus a fixed fee basis. Award fees, if applicable, for these contracts are recognized based upon historical performance or management estimates if no historical data is available.

The Company recognizes revenue on the Competitive Bidding Implementation Contractor (CBIC), Customer Support and Front End System (CSFES), Provider Education Support Service (PESS) and various other contracts when services are performed and billable.

Income taxes

Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates which are anticipated to be in effect when these differences reverse. The deferred tax provision is the result of the net change in the deferred tax assets to amounts expected to be realized. Valuation allowances are provided against deferred tax assets when the Company determines it is more likely than not that the deferred tax asset will not be realized.

The Company adopted the authoritative guidance on accounting for and disclosure of uncertainty in tax positions on January 1, 2009, which required the Company to determine whether a tax position of the Company is more likely than not to be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. For tax positions meeting the more likely than not threshold, the tax amount recognized in the financial statements is the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement with the relevant taxing authority. The tax position determination did not have a material effect on the Company's financial statements.

The Company files tax returns as prescribed by the tax laws of the jurisdictions in which it operates. In the normal course of business, the Company is subject to examination by federal and state jurisdictions, where applicable. As of December 31, 2017, the tax years 2014 forward remain subject to examination by the federal tax jurisdiction under the statute of limitations.

The Tax Cuts and Jobs Act of 2017 (TCJA) was signed into law on December 22, 2017, by President Donald J. Trump. The law includes significant changes to the U.S. corporate income tax system, including a federal corporate rate reduction from 35% to 21%, limitations on the deductibility of interest expense and executive compensation, and the transition of U.S. international taxation from a worldwide tax system to a territorial tax system.

Fair value measurements

The Company adopted the provision of Accounting Standards Codification (ASC) 820 effective 2009. ASC 820 establishes a framework for measuring the fair value of assets and liabilities recognized in the financial statements in periods subsequent to initial recognition.

NOTE 2

EQUIPMENT AND LEASEHOLD IMPROVEMENTS

Equipment and leasehold improvements consist of the following (in thousands):

	Years ended December 31, 2017	2016
Leasehold improvements	$ 232	$ 232
Equipment, furniture & fixtures	25,284	25,183
Software	9,131	9,054
	34,647	34,469
Accumulated depreciation	(31,242)	(30,842)
	$ 3,405	$ 3,627

Depreciation expense was $425,000 and $531,000 for the years ended December 31, 2017 and 2016, respectively.

NOTE 3

INVESTMENTS

Investments consist of the following (in thousands):

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2017				
Held-to-maturity securities:				
Corporate bonds	$ 16,713	$ 247	$ 191	$ 16,769
Mortgage-backed securities	7,372	37	122	7,287
Total held-to-maturity securities	24,085	284	313	24,056
Available-for-sale securities:				
Mutual funds	15,110	37	56	15,091
Total investments	**$ 39,195**	**$ 321**	**$ 369**	**$ 39,147**

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2016				
Held-to-maturity securities:				
Corporate bonds	$ 15,524	$ 153	$ 322	$ 15,355
Mortgage-backed securities	7,932	3	131	7,804
Total held-to-maturity securities	23,456	156	453	23,159
Available-for-sale securities:				
Mutual funds	5,132	–	55	5,077
Total investments	**$ 28,588**	**$ 156**	**$ 508**	**$ 28,236**

The Company monitors investment securities for other than temporary declines in fair value. In determining whether a decline in fair value is other than temporary, consideration is given to the extent of the decline, the length of time fair value has been below cost, and other relevant factors including estimated future cash flows. None of the unrealized losses at December 31, 2017 or 2016 were considered other than temporary.

The amortized cost and estimated fair values of held-to-maturity debt securities, by contractual maturity, at December 31, 2017, are as follows (in thousands):

	Amortized Cost or Cost Value	Fair Value
Held-to-maturity securities:		
Due in one year or less	$ –	$ –
Due in one year through five years	4,405	4,401
Due in five years or more	19,680	19,655
Total held-to-maturity	**$ 24,085**	**$ 24,056**

There were gross realized gains of $7,000 and $443,000 for the years ended December 31, 2017 and 2016, respectively, that were included in net investment income. There were gross realized losses of $56,000 and $294,000 for the years ended December 31, 2017 and 2016, respectively. Gross unrealized holding gains and losses on securities classified as available-for-sale are reported in accumulated other comprehensive income in the accompanying balance sheets. No cash or assets are pledged or restricted for any purpose.

For available-for-sale investments in an unrealized loss position at December 31, 2017, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was $56,000 and the aggregate estimated fair value was $7,482,000. There were no held-to-maturity investments in an unrealized loss position for more than twelve months at December 31, 2017. There were no available for-sale-investments that had been in an unrealized loss position for less than twelve months at December 31, 2016. For investments that had been in an unrealized loss position for more than twelve months, the aggregate amount of unrealized loss was $55,000 and the aggregate estimated fair value was $5,077,000.

For held-to-maturity investments in an unrealized loss position at December 31, 2017, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was $127,000 and the aggregate estimated fair value was $6,261,000. For investments that had been in an unrealized loss position for more than twelve months, the aggregate amount of unrealized loss was $186,000 and the aggregate estimated fair value was $6,061,000. For held-to-maturity investments in an unrealized loss position at December 31, 2016, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was $453,000 and the aggregate estimated fair value was $15,538,000. There were no investments in an unrealized loss position for more than twelve months at December 31, 2016.

FAIR VALUE MEASUREMENTS

The Company's financial assets carried at fair value have been classified, for disclosure purposes, based on a hierarchy defined by FASB. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). The levels of the fair value hierarchy are as follows:

Level 1 Values are unadjusted quoted prices for identical assets and liabilities in active markets accessible at the measurement date.

Level 2 Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are observable or can be corroborated by market data for the term of the instrument. Such inputs include market interest rates and volatilities, spreads and yield curves.

Level 3 Certain inputs are unobservable (supported by little or no market activity) and significant to the fair value measurement. Unobservable inputs reflect the Company's best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

FAIR VALUE OF ASSETS & LIABILITIES MEASURED ON A RECURRING BASIS (IN THOUSANDS)

	Level 1	Level 2	Level 3	Total
DECEMBER 31, 2017				
Mutual funds				
Publicly traded equities	$ 15,091	$ –	$ –	$ 15,091
Total Mutual funds	15,091	–	–	15,091
Total investments	**$ 15,091**	**$ –**	**$ –**	**$ 15,091**
DECEMBER 31, 2016				
Mutual funds				
U.S. Treasury obligations	$ –	$ 1,066	$ –	$ 1,066
Commercial mortgage-backed securities	–	355	–	355
Asset-backed securities	–	1,371	–	1,371
Agency obligations	–	508	–	508
Corporate bonds	–	1,624	–	1,624
Corporate International Sovereign	–	51	–	51
Registered investment company	102	–	–	102
Total Mutual funds	102	4,975	–	5,077
Total investments	**$ 102**	**$ 4,975**	**$ –**	**$ 5,077**

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

NOTE 4

INCOME TAXES

The Company's operations are included in the consolidated federal income tax return of BCBSSC. Under a written tax-sharing agreement, BCBSSC allocates the tax provision to each company within the consolidated group based upon the company's proportionate share of the consolidated federal income tax liability computed on a stand-alone basis, multiplied by the total consolidated federal income tax return liability.

The Company had income tax payables to BCBSSC of $1,674,000 and $2,205,000 at December 31, 2017 and 2016, respectively, which are included in net receivables and payables to the parent. The Company made payments to BCBSSC for income taxes of $6,352,000 and $6,124,000 during the years ended December 31, 2017 and 2016, respectively.

The Company recognized a provision for income taxes as follows (in thousands):

	Year ended December 31,	
	2017	2016
Current	$ 5,086	$ 5,320
Deferred	1,079	(705)
Total income taxes incurred	**$ 6,165**	**$ 4,615**

The provision for income taxes differs from the amount computed by applying the federal statutory tax rate of 35% to income before income taxes primarily due to changes in the tax contingency reserve, investment in subsidiaries, the dividends received deduction allowed for tax purposes, and the effect of reduced statutory rates as a result of the TCJA. We have recorded a deferred tax expense of $778,000 due to the re-measurement of deferred tax assets and liabilities resulting from the change in enacted corporate tax rates for years beginning after December 31, 2017. The temporary differences that give rise to deferred tax assets and liabilities are primarily related to accrued expenses, fixed assets, investments, and prepaid expenses. There was no valuation allowance at December 31, 2017 and 2016.

Deferred tax assets and liabilities are classified as current and long-term based on the classification of the related asset or liability, as follows (in thousands):

	December 31,	
	2017	2016
Deferred tax assets:		
Current	$ 1,880	$ 3,412
Long-term	4	35
	$ 1,884	**3,447**
Deferred tax liabilities:		
Current	$ 69	$ 46
Long-term	649	1,127
	$ 718	**$ 1,173**
Net deferred tax asset	$ 1,166	$ 2,274

NOTE 5

EMPLOYEE BENEFIT PLANS

The Company's employees are part of the 401(k) plan sponsored by BCBSSC. Eligible employees may defer up to 50% of their salary and the Company matched 50% of the first 6% deferred in 2017 and 2016. For employees hired after January 1, 2003, there is a 2-year cliff-vesting schedule on the match contribution. Employees hired after April 1, 2014, are not covered by the BCBSSC defined benefit pension plan. For those employees, the Company makes a discretionary contribution to the 401(k) plan which is 50% vested for employees with one year of service and fully vested for employees with two years of service. Employees must be employed on the last day of the year to be eligible for the discretionary contribution, unless terminated during the year due to retirement (age 55 and 5 years of service), death or disability. The discretionary Enhanced 401(k) contribution was 4% of salary for both years ended December 31, 2017 and 2016.

The cost of providing the 401(k) contribution was $3,160,000 and $2,726,000 for the years ended December 31, 2017 and 2016, respectively. The pension expense allocated to the Company under the BCBSSC defined benefit pension plan was $0 and $4,382,000 for the years ended December 31, 2017 and 2016, respectively.

NOTE 6

COMMITMENTS AND CONTINGENCIES

A financial guarantee has been issued by BCBSSC, which equals the Company's estimated annual net operating expenses multiplied by 8.33%, less current capitalization. This guarantee is estimated to be $0 at December 31, 2017. BCBSSC has also executed an indemnification agreement, pursuant to minimum reserve and other requirements established by the Blue Cross and Blue Shield Association (BCBSA). BCBSSC is, therefore, liable to the Company to the extent of its financial guarantee and to the BCBSA to the full extent of its assets for any claims asserted against the BCBSA resulting from the contractual and financial obligations of the Company arising out of its Medicare Part A subcontract with the BCBSA.

In consideration of the novation of the fiscal intermediary and carrier contracts from BCBSSC to the Company, BCBSSC has issued a financial guarantee which equals 20% of the administrative costs of the contracts contained in the Notice of Budget Approval, less current capitalization. This guarantee is estimated to be $0 at December 31, 2017. The financial guarantee agreement remains in effect until both the contracts and intermediary agreement expire, are non-renewed or are terminated, and closing agreements are executed.

In addition, BCBSSC has executed a statutorily required financial guarantee of $75,000 on behalf of the Company in order for the Company to obtain a Third Party Administrator's license pursuant to the South Carolina insurance laws.

The Company recorded an estimated contingent liability for potential repayments of costs claimed on its contracts with CMS. The liability was $4,334,000 and $5,348,000 at December 31, 2017 and 2016, respectively.

In the ordinary course of business, there are various legal proceedings pending against the Company. Management believes the aggregate liabilities, if any, arising from legal actions would not have a material adverse effect on the financial position of the Company.

NOTE 7

OPERATING LEASES

Lease expense under the operating leases was approximately $782,000 and $923,000 for the years ended December 31, 2017 and 2016, respectively. Future annual minimum lease payments as of December 31, 2017, under non-cancelable operating building leases, expiring in 2019, are as follows (in thousands):

Years ended December 31,	Amount
2018	$ 782
2019	522
Total	**$ 1,304**

NOTE 8

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

Restricted cash and cash equivalents and restricted cash liability increased by $671,000 in 2017 and $2,905,000 in 2016.

NOTE 9

RELATED PARTIES

The Company is a single-member limited liability company owned by BCBSSC. Certain offices, other facilities and services are provided by BCBSSC pursuant to an administrative services agreement. Expenses associated with the administrative services agreement allocated from BCBSSC to the Company totaled $66,526,000 and $57,981,000 for the years ended December 31, 2017 and 2016, respectively. The Company paid $66,593,000 and $67,480,000 during the years ended December 31, 2017 and 2016, respectively, to BCBSSC for expenses paid on behalf of the Company.

There are certain administrative services provided by the Company to BCBSSC and its subsidiaries. The Company received $16,971,000 and $14,866,000 for these services during the years ended December 31, 2017 and 2016, respectively.

The Company pays Companion Data Services (CDS, a wholly owned subsidiary of BCBSSC) fees for data analysis and data storage functions through usage of the Enterprise Data Center. The Company paid $2,200,000 and $1,404,000 for these services during the years ended December 31, 2017 and 2016, respectively.