

# UNCOMMON CARE

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PALMETTO GBA 2015 ANNUAL REPORT



**PALMETTO GBA®**

A CELERIAN GROUP COMPANY

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At Palmetto GBA, we refuse to accept good enough when great looms on the horizon. We relentlessly forge ahead, charting our own path not to what is but to what can be.

And yet, even as we adapt and improve our processes, we recognize that common courtesy, personal attention and a vested interest in our clients' wellbeing are the first steps toward true innovation. Our continued success will depend on the relationships we forge, the promises we keep, and the attention we devote to each and every assignment.

As we reflect on the 50th anniversary of Medicare's implementation, we renew our pledge to protect the health, security and independence of millions of Americans. And, as we look forward to all the future's grand possibilities, we do so with **UNCOMMON CARE.**

# PRESIDENT'S LETTER

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**PALMETTO GBA®**

A CELERIAN GROUP COMPANY

In the coming years, maintaining our market position as a leader in the field of Medicare administration will be no easy task. It will require vision and ingenuity, resilience in the face of challenges and a relentless drive to improve upon yesterday's performance. It will require an unwavering focus on our strategic plan and the know-how to achieve our goals. And, it will require one other, equally essential ingredient: dedication to the work we do.

Customers recognize sincerity and genuine concern when they see it. Whether going the extra mile to resolve a claim or working overtime to fulfill a tight deadline, I believe it's our shared vision to improve the lives of our customers and our communities that ultimately sets Palmetto GBA apart from the competition.

In looking for new ways to best serve our clients, we aspire to the very highest of standards. Every day, our associates exceed expectations by looking for new ways to work more efficiently and provide customers with an even better level of performance. The outcomes of our innovations have been of great interest to our customers, and many are currently being shared as new industry standards.

Our personal attention to customers' needs has also yielded success in our business development activities, where we continue to make strides. I am excited by the opportunities and contracts we have been awarded, and I feel we are well positioned for future growth.

Truly, it is our associates who are responsible for facilitating the thousands of daily interactions that have made this year's achievements possible. I continue to be grateful to work with people who so selflessly give of their time, talents and resources on behalf of this great organization.

Best regards,

Walter J. Johnson  
President and COO



# COMPANY OVERVIEW

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

As a Medicare contractor with 50 years of experience, Palmetto GBA has been entrusted with administering health insurance claims for many of our nation's elderly and disabled citizens since the inception of the Medicare Program. Headquartered in Columbia, SC, the company employs more than 1,500 associates throughout the United States. In 2015, the organization served approximately 7.6 million beneficiaries, processing 113 million claims and paying more than \$41.8 billion in benefits.

DOLLARS IN  
BENEFITS PAID

41.8  
BILLION

CLAIMS  
PROCESSED

113  
MILLION

BENEFICIARIES  
SERVED

7.6  
MILLION

INQUIRES  
ANSWERED

1.1  
MILLION

# A SOLEMN PROMISE

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On July 30, 1965, President Johnson signed the Social Security Amendments that established Medicare and Medicaid, providing health care to millions of people regardless of their income or medical history. In his remarks to the crowd gathered before him, he stated, “Many men can make proposals. Many men can draft laws. But few have the piercing and humane eye which can see beyond the words to the people they touch.”

Although Johnson’s words were uttered in praise of President Harry Truman, the man whom he credited with planting the “seeds of compassion and duty” that became modern Medicare, the same words could be spoken of the people here at Palmetto GBA. While ever mindful of the rules and stated requirements, our associates also possess that rare, piercing and humane ability to see past the contract to the lives affected by its successful fulfillment.

Whether automating a manual process or innovating to better safeguard the Medicare Trust Fund, our associates know there’s far more at stake than just the bottom line. We know the measure of true performance, of tasks completed with diligence, determination and attention to detail. We know the impact of our work on the health of a beneficiary, a stranger who could just as easily be a parent or friend. And, we know the power of a small act to change a life.

That’s why we take the time to ensure every “i” is dotted and “t” is crossed before beginning again tomorrow, why we ask not what we can do for our clients but how we can help them reach their goals. Because, while Medicare funds medical miracles unfathomable in 1965, Johnson’s call to “maintain and to improve the health of all Americans” is no less paramount now than it was 50 years ago. As the program continues to grow and evolve, know that Palmetto GBA will be there too, working with uncommon care to reduce costs, improve efficacies and lead the way toward a brighter future for the beneficiaries we serve.

“Many men can make proposals. Many men can draft laws. But few have the piercing and humane eye which can see beyond the words to the people they touch.”

**LYNDON B. JOHNSON**



## OUR MISSION

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Palmetto GBA creates value for government and commercial customers by continuously transforming ideas into technical and administrative solutions that improve service, quality and cost.

## OUR VISION

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To be the most essential organization to our customers in reaching new heights of performance, ultimately improving the quality of life of our customers, our employees, and our communities.

# TAKING CARE

Talk to any Palmetto GBA associate, and one thing becomes immediately clear: we put people first. The following conversations are testament not only to the myriad ways our associates find meaning and value in their individual tasks, but also their common desire to care for the clients and communities we serve.

## CONVERSATIONS WITH



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**paige easley**  
SYSTEM SECURITY OFFICER

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**brittany dodgen**  
APPEALS SPECIALIST

**harriett shepherd**  
TRAINING MANAGER

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**jim peebles**  
REIMBURSEMENT MANAGER

**bonnie castillo**  
ACCOUNTING MANAGER

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**alex delage**  
STATISTICAL RESEARCH MANAGER

**cheryl bolchoz**  
STATISTICAL PROGRAMMING ANALYST

**renee simeon**  
STATISTICAL PROGRAMMING ANALYST

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**glenda piatt**  
CLAIMS PROCESSING DIRECTOR

**lovealee blevins**  
OPERATIONS ANALYST

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**daliyl skinner**  
SUPPLIER CONTRACTING ANALYST

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**shannon chase**  
PROVIDER RELATIONS REPRESENTATIVE

**jazz harrison**  
PROVIDER EDUCATION CONSULTANT

A CONVERSATION WITH



paige easley



**You've been in this business a long time. Why is security so important, and what major changes have you witnessed?**

**Paige:** At Palmetto GBA, we're protecting millions of medical records from falling into the wrong hands. We have to be vigilant. Our standards have to be exacting. And they are. They're what led us to develop Security Manager, our award-winning in-house software. We've transformed what were time-consuming manual processes prone to human error into automated processes. So now, when the program alerts us to a potential vulnerability, we have the manpower available to immediately diffuse any threat to beneficiaries' personal information. There's an umbrella of protection over everything we do here.

**What hasn't changed?**

**Paige:** At the end of the day, what we do is still an exercise in common sense. Think about when you go on a long car trip: you check your tire pressure, make sure you have your license, fill up with gas, and then you hit the road. Security follows a similar rule set of checks and protocols. The way risks are identified and addressed may be completely digitized now, but we're still in the business of ensuring we're prepared for safe passage.

A CONVERSATION WITH



**brittany dodgen**  
**harriett shepherd**



**In October, a “once in a thousand years” flood devastated parts of Columbia, South Carolina, where Palmetto GBA is headquartered. In what ways did you see associates come together to support relief efforts?**

**Brittany:** In the days after the flood, the company asked us if we had been affected—there was an immediate desire to identify and take care of people within our own organization. I took a lot of comfort in seeing those emails and knowing that the company’s concern matched mine.

**Harriett:** We really had the full support of senior leadership, who were quick to act and ask how our organization could be part of rebuilding this community that we all love. As the chair of my division’s community service committee, I called every organization I knew was involved in relief to learn what their needs were and figure out how we could help as a team.

**Brittany:** The flood touched everyone on a different level, but—whether it was volunteering or donating clothes or just being there to listen and offer support—it seemed like everyone in our department found a way to rally around our community that was hurting.

**Harriett:** Ultimately, our response to the flood was just one demonstration of our people living out our corporate vision to improve the lives of our customers, coworkers and communities. I think that’s such a profound statement, because we really are trying to do what we say and say what we do. It’s an obligation that goes beyond work—we are our brothers’ and sisters’ keepers.

**As more beneficiaries come into the Medicare fold, it's become imperative that companies like Palmetto GBA find new ways to protect the Medicare Trust Fund. How are you evolving to save government dollars?**

**Jim:** Our RAP [Request for Anticipated Payment] suppression program helps us stay one step ahead of providers who try to abuse CMS's billing system.

Because we have more ways of analyzing the data now than we had five or 10 years ago, we're able to identify patterns and red flags that lead us to fraudulent billers sooner. The more we do this and refine our review processes, the better we're able to drill down to identify questionable billing. Our processes continue to improve as we focus on preventing incorrect RAP payments and protecting the Trust Fund.

**Bonnie:** This is something that no one else is doing, and it has a tangible, money-saving benefit for the government. We've really shifted our focus from correcting overpayments to avoiding them in the first place. Since we started suppressing RAPs, we estimate that we've saved the Medicare Program more than 72 million dollars.

*To learn more about the continued evolution of the RAP suppression program, see page 20.*

A CONVERSATION WITH



**jim peebles**  
**bonnie castillo**



A CONVERSATION WITH



**alex delage**  
**cheryl bolchoz**  
**renee simeon**



**As data analysts, how do you collaborate with other departments to bring about process improvements and high-level organizational change?**

**Alex:** Across the board, our associates truly care about the work they do and want to make our processes better. Our team facilitates that effort. And, just given what we're capable of and the amount of information we can glean through analysis, there's so much we can do to help. It seems like it's every day that someone in another department realizes we can help them cull new insights from the data they're collecting.

**Renee:** We're also working in close proximity to the nurses who are responsible for talking to providers. We ask questions, they ask questions—we're constantly learning from one another. Then, we're refining our code based on those exchanges.

**Cheryl:** I think it's also true that, in a lot of cases, we're coming to other departments with suggestions, even when we don't have a direct purpose on their contract. We're always researching new trends, scanning news publications to see where medical policy is headed next and mining the data deeper and deeper to uncover patterns that can help our coworkers do more for CMS. As unlikely as it sounds, this kind of puzzle solving is fun, especially when we're able to educate providers and improve their experience.

**How do the most recent automated enhancements your claims processing team has implemented ultimately benefit CMS?**

**Glenda:** It's all about making the most of our resources. Anywhere we can, we're looking for ways to continually save budget dollars and reduce the risk of human error. By automating what were manual functions and writing scripts that electronically funnel claims through our database, we're eliminating processes that don't add value. Our staff is made up of people who are thinkers and analysts, and they're making key decisions in the lifespan of a claim.

**Lovealee:** By getting rid of hardcopies, we're cutting down on the expense of storing paper files. We're adding a layer of security. We're saving our support staff's time so they can get to the things that truly matter. And, this way, we know nothing is going to be left undone. We can track everything we do in real time, see trends, find repetitive functions and then use all of that information to improve the quality of our work.

**Glenda:** There's always something more we can do, and our eyes are open to those opportunities. At Palmetto GBA, we never settle because we want to be the very best we can be for our customers.

A CONVERSATION WITH



**glenda piatt**  
**lovealee blevins**



## UNMATCHED COMMITMENT



A CONVERSATION WITH  daliyl skinner

**In working on the Competitive Bidding Implementation Contract, where do you see the end results of your day-to-day efforts?**

**Daliyl:** Our team is responsible for evaluating pharmacies and other medical suppliers to verify that they're licensed and in good standing. The review process gives everyone from small businesses to Fortune 500 companies the opportunity to win contracts. And the more companies we bring in, the more options a Medicare beneficiary has to choose from. I feel like we're supporting the health of entire communities by ensuring businesses can open their doors, especially in underserved locations. This way, regular people, people like my grandmother and my dad, have access to the medicines they need.

**How does that perspective and care shape Palmetto GBA's corporate culture?**

**Daliyl:** I think knowing that what we're doing affects people's lives translates into a willingness to go above and beyond, you see that at every level of the company. You know, when we have deadlines to meet, we're working weekends and late nights right alongside our managers. Leadership is coming through to sit down and understand the processes behind the work that those of us in the middle are responsible for. It feels good when I attend meetings where my opinions are asked for and valued. We're all putting in the extra effort, and to me that's what sets us apart.

**Through the Organizational Process Improvement Coaching Project (OPICP), you've been working with ambulance providers and their referral sources to implement CMS's changes to prior authorization and improve their organizational processes. What's been most meaningful about this work?**

**Jazz:** The prior authorization requirement didn't change documentation regulations, but it did change when documentation had to be submitted for non-emergent ambulance transports. Our goal with this project was to improve prior authorization approvals the first time around and help care providers navigate this new process. Ambulance providers fill a critical role, and it's been a real labor of love to walk this journey with them. They know now that we're listening and working in their best interests. And, that we're ultimately working to ensure beneficiaries get the care they need.

**Shannon:** We know change can be uncomfortable, and we're dedicated to making this transition successful for all of the stakeholders involved. Using the Lean Six Sigma process, we were able to work through organizational processes with our provider volunteers to figure out the best approach. Our feet are on the ground to reach providers, and we've remained persistent because we're dedicated to this work. I think with any implementation there are going to be kinks to work out, but we're here to be part of a bigger solution.

A CONVERSATION WITH



shannon chase  
jazz harrison



# PERFORMANCE

At Palmetto GBA, our relentless pursuit of excellence is bolstered by our attention to the smallest details, commitment to surpassing the status quo and deep-seated desire to add value to our customers' operations. These are the hallmarks of uncommon care, and they continue to yield opportunities for unprecedented levels of achievement.

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## **BUSINESS DEVELOPMENT**

### **Jurisdiction M (JM) A/B MAC**

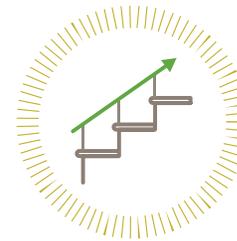
On April 1, 2015, Palmetto GBA was awarded the Jurisdiction M A/B MAC (formerly Jurisdiction 11 A/B MAC) contract. Jurisdiction M includes the states of North Carolina, South Carolina, Virginia and West Virginia, as well as a 16-state home health and hospice region. The JM A/B MAC implementation was successfully completed on August 27, 2015.

### **Program Support Center (PSC)**

On March 17, 2015, Palmetto GBA, as a subcontractor to Battelle Memorial Institute, was awarded the Department of Health and Human Services (DHHS) National Institutes of Health Program Support Center Indefinite Delivery Indefinite Quantity (IDIQ) contract. The task orders under the IDIQ contract will involve a range of health IT and information policy services including, but not limited to, the following supports: health policy and program analysis or assessments; evaluations, design, data collection and implementations; and technology and software support, data analysis and technical expertise.

### **CMS Survey and Certification Group (SCG) National Surveyor Training Program (NSTP) IDIQ**

On May 28, 2015, Palmetto GBA, as a subcontractor to CAS Consultants, Inc., was awarded the SCG NSTP IDIQ contract. The purpose of this contract is to provide training on a variety of Health Care Survey & Certification Processes for the CMS Central Office Survey and Certification Group.



**PALMETTO GBA**  
SINCE 1998

## INNOVATIONS & ENHANCEMENTS



### Advanced Clinical Editing (ACE)

Palmetto GBA integrated the Optum ACE solution with our Electronic Data Interchange (EDI) front-end claims-processing system and the CMS Common Edit Module (CEM). This software performs complex claim editing within the EDI front-end process and before adjudication. Scripted edits will reject claims likely to be denied based on existing policies, program guidance, correct coding, and other published articles. By applying these edits in the EDI stream and rejecting the claim, the system prevents unnecessary appeals and inquiries related to these denials and adjudication system rejects.

The most powerful component of this tool is its communication integration into the EDI data stream. ACE messages are added to the transaction file as “smart edits.” These ACE smart edits use plain and direct language to detail errors, allowing providers to withdraw, correct and/or resubmit an accurate claim. The ACE product incorporates more than 12 million edit parameters built from a compilation of published Medicare guidance, along with general coding guidance. ACE enables immediate and very specific feedback to providers, translating to a significant decrease in claim payment turnaround.

In addition to these clinical/policy edits, ACE includes the ability to use claims history and apply pattern-detection editing. These pattern-detection edits compare historical claims information with the current claim submitted to identify unlikely billing behaviors based on this historical knowledge. Palmetto GBA experienced the outcomes detailed below in the first year of the pilot project.

17%

OF REJECTED CLAIMS  
WERE NOT RESUBMITTED

(\$104.5 MILLION IN CHARGES)

42%

OF REJECTED CLAIMS WERE  
RESUBMITTED WITH CORRECTIONS

(\$52.6 MILLION LESS TOTAL CHARGES)

## INNOVATIONS & ENHANCEMENTS

### Cognitive Medical Review System (CMRS)

Palmetto GBA developed CMRS in 2012 to extend our existing medical review systems platform and to increase the effectiveness of our medical review, Comprehensive Error Rate Testing (CERT) and provider outreach and education processes beyond contractual requirements. CMRS sets our medical review process apart from our national competitors, as it focuses on using enhanced data analytics and technology to target and refine our efforts, accelerate cycle times, enhance education efforts and achieve desired performance outcomes rapidly.

CMRS captures and identifies patterns of errors in claims submissions and payments with increasing efficiency and effectiveness. It “learns” provider billing and error patterns. In 2015, enhancements to CMRS included increased responsiveness between CMRS and the Provider Outreach and Education Tracking System, improvements to the medical review denial process, automation of post-pay edit creation process and a new function that allows for the in-system creation of beneficiary edits.



### Suite of eServices

Palmetto GBA's eServices provider portal continues to be the most used and feature-rich CMS MAC portal, empowering the provider community with a range of self-service tools. This innovation expands our portal functionality to include features like claims status, eligibility, remittance information, and financial tools. With our latest generation of features, the portal now offers providers an eServices suite fully integrated with Palmetto GBA's internal systems and the Medicare standard systems. This offers providers a complete channel to obtain information, conduct independent research, complete financial transactions and directly interface with all Palmetto GBA functional areas through controlled workflow processes. Ours is a true two-way channel, facilitating communication that can be originated by either party and/or communication in which two parties can actively exchange information.

These self-service electronic exchanges, plus their direct integration with systems and our workflow management tools, eliminate manual processing of documents, reduce calls and improve customer satisfaction.



## INNOVATIONS & ENHANCEMENTS



### **Molecular Diagnostic Services Program (MoIDX®)**

Developed in 2011, MoIDX identifies and establishes coverage and reimbursement for molecular diagnostic tests. MoIDX hinges on three components: (1) test registration; (2) application review of existing tests for correct coding, coverage, and pricing; and (3) a technical assessment of new tests for clinical utility and analytical and clinical validity. Educational articles, Local Coverage Determinations (LCDs), and edits are then developed to manage these tests.

In addition to the MoIDX-specific CPT code range, the MoIDX program reviews and provides education on all pathology-related issues including, but not limited to, controlled substance monitoring, circulating tumor cell markers, and immunohistochemistry. To date, more than 4,900 lab tests have been registered, and the Medicare program cost avoidance totals more than \$843 million.

### **Debt Management System (DMS)**

Palmetto GBA continues implementation of a comprehensive Medicare Debt Management System (DMS). Palmetto GBA has implemented a series of operational modules that will streamline and allow for efficiencies in processing and managing Medicare debts throughout a debt's life cycle. From January 2015 through December 2015, DMS processed an average of 68.22 percent of overall financial keying and keying QC volume, with over 150,000 transactions processed for this same period.

Beginning in 2015, additional modules were implemented in DMS for Bankruptcy, Appeals, Extended Repayment Schedules and Check Application. The implementation of these new modules continues to expand the integration of Palmetto GBA's Medicare debt oversight across operational areas. All new modules are integrated with the Healthcare Integrated General Ledger Accounting System (HIGLAS) Automator, allowing for accurate and timely updates of financial transactions from DMS to HIGLAS. A framework has also been put in place to expand the reach of DMS to include other divisions within Palmetto GBA as well as integrate DMS with Palmetto GBA's eServices application. Both of these initiatives will increase the visibility and accessibility of Medicare debt management to the provider community, further enhancing Palmetto GBA's commitment to superior customer service.

## INNOVATIONS & ENHANCEMENTS

### Security Manager Application

The Security Manager Application continues to automate security and compliance requirements and reviews. In the last year, over 30 enhancements have been made to the application. Security Manager has not only improved security and compliance, but also has resulted in a net savings of 7,000 man-hours each year.



### Request for Anticipated Payment (RAP) Suppression Enhancements

Palmetto GBA's RAP suppression innovation continues to produce savings for the Medicare Program. A RAP is an initial partial payment—usually about 50 percent—of the expected total Medicare final claim for a home health episode. Providers are required to file a final claim for the actual services rendered, reconciling the claim. By monitoring billing practices to identify providers that do not submit final home health bills, overpayments to providers are avoided. Beginning in 2013, Palmetto GBA developed criteria to identify providers whose billing processes were questionable and established protocols to address payment issues.

In the spring of 2015, the RAP Suppression program underwent significant enhancement. Realizing that existing processes identified problematic providers after payments had been made, we saw the opportunity to improve our monitoring process and stop overpayments earlier. By developing weekly reports to flag questionable behavior as RAPs were submitted, Palmetto GBA is able to run more frequent targeted reports, catching fraudulent activity before funds have even left the building. This new weekly process resulted in approximately \$8.7 million in savings for the Medicare Program during the last nine months of 2015.

## ACCOMPLISHMENTS

### Medicare Integrity Program

Our program safeguard activities result in significant savings for Medicare. For the calendar year 2015, Palmetto GBA's efforts resulted in the Medicare savings detailed below:

	J11(M) A/B MAC	RRB SMAC
BI	N/A	\$ 1,111,851
MSP	\$ 481,641,249	\$ 5,160,995
MR	\$ 576,756,635	\$ 17,177,888
<b>TOTAL</b>	<b>\$ 1,058,397,884</b>	<b>\$ 23,450,734</b>

BI Benefits Integrity  
MSP Medicare Secondary Payer  
MR Medical Review

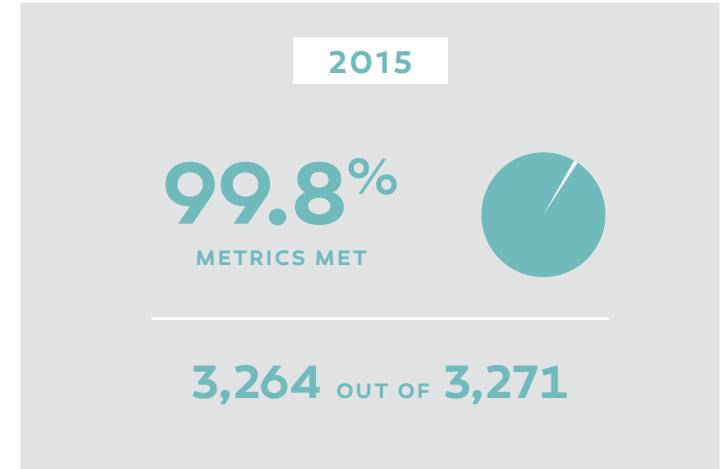
\*For J11(M) A/B MAC the figure is for Part A, HHH, and Part B combined.

### nCircle IP360 Scores

Palmetto GBA continues to focus on the overall compliance of our systems security program. Palmetto GBA's IP360 system security scores maintained an "A" rating for the past consecutive 27 months. Palmetto GBA has consistently had one of the best scores each month of any CMS contractor.

### Exceptional Performance Metrics

Palmetto GBA's performance across all contract metrics in 2015 was 99.8 percent.



## CORPORATE SOCIAL RESPONSIBILITY

In keeping pace with business as usual, we never forget to care for those around us. We reach out to customers, ensuring they feel heard in their concerns and appreciated in the solutions we devise on their behalf. And, we look beyond our own walls to the hard work of our peers, the needs of our neighbors, and the responsibility we share to help those less fortunate whenever and however possible.

In realizing that what we do impacts not only the beneficiaries we serve, but also each and every member of the communities we call home, we dedicate ourselves to a higher standard of service. At Palmetto GBA, giving back is neither a business obligation nor a superficial endeavor. Rather, it is an essential element of our company DNA. In each item donated, dollar raised and volunteer hour spent, our associates' compassion for others is evident, their desire to make a difference clear. Taken together, these personal acts of uncommon care add to a profound statement of corporate generosity.

2015

2,700

dollars raised through bake sales and “jeans days” for *Relay for Life*

DIVISION 96: AUGUSTA OPERATIONS

360

pounds of food and toiletries donated to the *Mid-Ohio Food Bank*

DIVISION 05: OHIO OPERATIONS

137

dresses donated to pediatric cancer patients attending *Camp Kemo’s Valentine Ball*

DIVISION 54: FINANCE AND ACCOUNTING

48

degree weather, plus ice cold waters braved during the *Special Olympics’ Polar Plunge*

DIVISION 1M: MoLDX, PROVIDER EDUCATION SUPPORT SERVICES, NATIONAL SUPPLIER CONTRACTOR MAC, RAILROAD BOARD SMAC

10

fifth graders mentored through the *Joseph Keels Elementary Table Talkers Program*

DIVISION 10: COMPETITIVE BIDDING IMPLEMENTATION CONTRACTOR

6

high school seniors inspired during shadowing days hosted in conjunction with the *University of SC’s Partners for Minorities in Engineering & Computer Science Program*

DIVISION 34: SYSTEMS AND SUPPORT DIVISION

4

lives brightened through the team’s gifts and donations to *Families Helping Families*

DIVISION 28: JURISDICTION M A/B MAC OPERATIONS

1

day of painting, building and carpentry on behalf of *Habitat for Humanity*

DIVISION 42: FACILITY SUPPORT OPERATIONS



infinite acts of kindness, community service and support during Columbia’s flood relief efforts

ALL DIVISIONS

# LEADERSHIP

## BOARD OF DIRECTORS



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RETIRED

*Strategic Management Systems*



**BRUCE W. HUGHES**

PRESIDENT & COO

*Celerian Group*



**WALTER J. JOHNSON**

PRESIDENT & COO

*Palmetto GBA, LLC*



**MARTIN L. KAPPERT**

RETIRED

*CMS & Department of Defense*



**ILENE H. NAGEL**

MANAGING DIRECTOR

*Russell Reynolds Associates*



**DAVID PANKAU**

CHAIRMAN,  
BOARD OF DIRECTORS

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PRESIDENT/CEO

*BlueCross BlueShield of South Carolina*



**BRIAN RUBIN**

RETIRED

*Department of Defense*

*TRICARE Management Activity*



**M. EDWARD SELLERS**

CHAIRMAN,  
BOARD OF DIRECTORS

*BlueCross BlueShield of South Carolina*



**JOSEPH F. SULLIVAN**

CHAIRMAN EMERITUS,  
BOARD OF DIRECTORS

*BlueCross BlueShield of South Carolina*

# LEADERSHIP

## CORPORATE OFFICERS



**MIKE BARLOW**  
VICE PRESIDENT  
*Operations, Specialty Contracts*



**NELLA BISHOP**  
CIO & VICE PRESIDENT  
*Systems & Support*



**NEAL BURKHEAD**  
VICE PRESIDENT  
*Shared Services*



**ELAINE GARRICK**  
VICE PRESIDENT  
*Support Operations*



**WALTER J. JOHNSON**  
PRESIDENT & COO



**KEN LEWIS**  
VICE PRESIDENT & CFO



**LEE MCELVEEN**  
VICE PRESIDENT  
*Compliance & Privacy*



**MIKE MIZEUR**  
TREASURER



**DEDEE ROWE**  
SECRETARY



**ED SANCHEZ**  
VICE PRESIDENT  
*Jurisdiction M A/B  
MAC Operations*

# FINANCIAL REPORT

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## INDEPENDENT AUDITOR'S REPORT



ACCOUNTING • AUDITING • TAXATION • CONSULTING

TEL 803.799.5810 | POST OFFICE BOX 36 | COLUMBIA, SC 29202-0036  
T-F 866.799.5810 | 508 HAMPTON ST, 1<sup>ST</sup> FLOOR | COLUMBIA, SC 29201  
FAX 803.799.5554 | DSSCPA.COM

### BOARD OF DIRECTORS PALMETTO GBA, LLC

#### Report on the Financial Statements

We have audited the accompanying financial statements of Palmetto GBA, LLC which are comprised of the balance sheets as of December 31, 2015 and 2014, and the related statements of operations, comprehensive income, changes in member's equity, and cash flows for the years 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 audits. We conducted our audits 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, 2015 and 2014, 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.

*Derrick, Stubbs & Stith, LLP*

February 29, 2016

**BALANCE SHEETS** (IN THOUSANDS)

December 31,

2015                      2014

**ASSETS****Current assets:**

Cash and cash equivalents	\$ 46,078	\$ 27,201
Restricted Medicare Funds	744	540
Accounts receivable	28,187	41,161
Accounts receivable from affiliates	1,658	1,235
Accrued revenue	41,361	40,119
Prepaid expenses	686	1,959
Deferred income taxes	2,826	3,055
<b>Total current assets</b>	<b>121,540</b>	<b>115,270</b>

**Long-term assets:**

Fixed assets, <i>net of accumulated depreciation of \$30,439 and \$29,931 in 2015 and 2014, respectively</i>	3,794	4,153
Long-term investments	13,080	8,121
Investments in affiliates	1,831	1,785
Deferred income taxes	30	-
<b>Total long-term assets</b>	<b>18,735</b>	<b>14,059</b>

**TOTAL ASSETS**

<b>\$ 140,275</b>	<b>\$ 129,329</b>
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**LIABILITIES AND MEMBER'S EQUITY****Current liabilities:**

Accrued payroll, taxes and benefits	\$ 13,489	\$ 12,966
Payable to parent	7,460	6,916
Restricted Medicare Funds	744	540
Other liabilities	12,962	14,336
Deferred income taxes	117	261
<b>Total current liabilities</b>	<b>34,772</b>	<b>35,019</b>

**Long-term liabilities:**

Deferred income taxes	<b>1,175</b>	<b>1,293</b>
<b>Total long-term liabilities</b>	<b>1,175</b>	<b>1,293</b>

**Member's equity:**

Contributed capital	34,961	34,961
Retained earnings	69,424	57,998
Accumulated other comprehensive income	(57)	58
<b>Total member's equity</b>	<b>104,328</b>	<b>93,017</b>

**TOTAL LIABILITIES AND MEMBER'S EQUITY**

<b>\$ 140,275</b>	<b>\$ 129,329</b>
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**STATEMENTS OF OPERATIONS** (IN THOUSANDS)

	Years ended December 31,	
	2015	2014
<b>REVENUES</b>		
Total revenues	\$ 213,118	\$ 212,232
<b>EXPENSES</b>		
Total expenses	195,755	200,583
Gain from operations	17,363	11,649
Investment income	167	200
Income before income taxes	17,530	11,849
Provision for income taxes	6,104	4,123
<b>NET INCOME</b>	<b>\$ 11,426</b>	<b>\$ 7,726</b>

**STATEMENTS OF COMPREHENSIVE INCOME** (IN THOUSANDS)

	Years ended December 31,	
	2015	2014
<b>NET INCOME</b>	\$ 11,426	\$ 7,726
Other comprehensive income (OCI), net of tax		
<b>Unrealized gains on investments:</b>		
Unrealized holding (loss)/gain arising during period, net of (\$61) tax benefit and \$20 tax expense in 2015 and 2014	(115)	38
<b>Total unrealized gains on investments</b>	<b>(115)</b>	<b>38</b>
Other comprehensive income	(115)	38
<b>COMPREHENSIVE INCOME</b>	<b>\$ 11,311</b>	<b>\$ 7,764</b>

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

	Contributed Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balance January 1, 2014	\$ 34,961	\$ 50,272	\$ 20	\$ 85,253
Net income	-	7,726	-	7,726
Other comprehensive income	-	-	38	38
Balance December 31, 2014	34,961	57,998	58	93,017
Net income	-	11,426	-	11,426
Other comprehensive income	-	-	(115)	(115)
Balance December 31, 2015	<b>\$ 34,961</b>	<b>\$ 69,424</b>	<b>\$ (57)</b>	<b>\$ 104,328</b>

## STATEMENTS OF CASH FLOWS (IN THOUSANDS)

	Years ended December 31,	
	2015	2014
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 11,426	\$ 7,726
<b>Adjustments to reconcile net income to net cash provided by (used in) operating activities:</b>		
Depreciation	618	848
Amortization on bonds	21	32
Loss on fixed asset disposals	13	61
Realized loss on investments	100	(34)
Unrealized gain on investments	176	(59)
Change in other comprehensive income	(115)	38
Equity in income of affiliates	(46)	(59)
Deferred income tax provision	(63)	(107)
<b>Changes in operating assets and liabilities:</b>		
Decrease (increase) in accounts receivable	11,732	(9,976)
(Increase) decrease in receivables from affiliates	(423)	1,074
(Increase) in accrued revenue	-	(3,471)
Decrease in prepaid expense	1,273	224
Increase (decrease) in accrued payroll, taxes and benefits	523	(2,108)
Increase (decrease) in payable to parent	544	1
(Decrease) increase in other liabilities	(1,374)	67
<b>Net cash provided by (used in) operating activities</b>	<b><u>24,405</u></b>	<b><u>(5,743)</u></b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Fixed assets purchased	(272)	(291)
Investments redeemed - held-to-maturity	564	661
Investments sold - available-for-sale	1,136	339
Investments purchased - held-to-maturity	(2,654)	-
Investments purchased - available-for-sale	(4,302)	(1,157)
<b>Net cash (used in) investing activities</b>	<b><u>(5,528)</u></b>	<b><u>(448)</u></b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>18,877</b>	<b>(6,191)</b>
<b>Cash and cash equivalents beginning of year</b>	<b>27,201</b>	<b>33,392</b>
<b>Cash and cash equivalents end of year</b>	<b><u>\$ 46,078</u></b>	<b><u>\$ 27,201</u></b>
<b>Supplemental disclosures of cash paid during the year for:</b>		
Income taxes	\$ 6,260	\$ 3,101

**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 \$744,000 and \$540,000 at December 31, 2015 and 2014, 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 \$46,279,000 and \$27,676,000 at December 31, 2015 and 2014, respectively.

**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 February 29, 2016, 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.

### Fixed assets

Fixed assets 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, 2015 and 2014.

### 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.

## ASSETS, LIABILITIES & RESULTS OF OPERATIONS FOR TRICENTURION, INC.

(IN THOUSANDS)

	Years ended December 31,	
	2015	2014
Assets	\$ 12,931	\$ 12,670
Liabilities	\$ 5,639	\$ 5,533
Net Income	\$ 155	\$ 237

## **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 and Railroad Retirement Board SMAC 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**

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, 2015, the tax years 2012 forward remain subject to examination by the federal tax jurisdiction under the statute of limitations.

If applicable, the Company accrues interest and penalties that may be assessed by the taxing authorities on any underpayment of tax. As of December 31, 2015, the Company had not accrued any interest and penalties related to income tax accruals.

## **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.

## **PRIOR YEAR RECLASSIFICATIONS**

Certain 2014 amounts have been reclassified on the balance sheet and in the notes in order for them to be comparable with the 2015 amounts. These reclassifications resulted in no change to net income or member's equity.

## **NEW PRONOUNCEMENTS**

The FASB issued ASU 2014-09, Revenue from Contracts with Customers, which is expected to remove inconsistencies and weaknesses in revenue requirements and improve comparability of revenue recognition practices across companies, industries, jurisdictions and capital markets. ASU 2014-09 is effective for fiscal periods beginning after December 15, 2017. The Company is currently evaluating ASU 2014-09 but does not expect it will have a material impact on the Company's results of operations, cash flows or financial position.

The FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date. The amendments in ASU 2015-14 defer the effective date of ASU 2014-09.

## NOTE 2 FIXED ASSETS

### FIXED ASSETS (IN THOUSANDS)

	Years ended December 31,	
	2015	2014
Leasehold improvements	\$ 231	\$ 222
Equipment, furniture & fixtures	25,294	25,359
Software	8,708	8,503
	<u>34,233</u>	<u>34,084</u>
Accumulated depreciation	(30,439)	(29,931)
	<u>\$ 3,794</u>	<u>\$ 4,153</u>

Depreciation expense was \$618,000 and \$848,000 for the years ended December 31, 2015 and 2014, respectively.

## NOTE 3 INVESTMENTS

### LONG-TERM INVESTMENTS (IN THOUSANDS)

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>DECEMBER 31, 2015</b>				
<b>Held-to-maturity securities:</b>				
Corporate bonds	\$ 4,017	\$ 15	\$ 71	\$ 3,961
<b>Total held-to-maturity securities</b>	<b>4,017</b>	<b>15</b>	<b>71</b>	<b>3,961</b>
<b>Available-for-sale securities:</b>				
Common stocks	4,036	205	224	4,017
Mutual funds	5,071	–	25	5,046
<b>Total long-term investments</b>	<b>\$ 13,124</b>	<b>\$ 220</b>	<b>\$ 320</b>	<b>\$ 13,024</b>
<b>DECEMBER 31, 2014</b>				
<b>Held-to-maturity securities:</b>				
Corporate bonds	\$ 1,991	\$ 49	\$ 1	\$ 2,039
<b>Total held-to-maturity securities</b>	<b>1,991</b>	<b>49</b>	<b>1</b>	<b>2,039</b>
<b>Available-for-sale securities:</b>				
Common stocks	1,000	134	25	1,109
Mutual funds	5,041	–	20	5,021
<b>Total long-term investments</b>	<b>\$ 8,032</b>	<b>\$ 183</b>	<b>\$ 46</b>	<b>\$ 8,169</b>

The fair value of available-for-sale securities with unrealized losses was \$7,167,000 and \$5,248,000 at December 31, 2015 and 2014, respectively. 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, 2015, were considered other than temporary.

**AMORTIZED COST & ESTIMATED FAIR VALUES  
OF HELD-TO-MATURITY DEBT SECURITIES, BY  
CONTRACTUAL MATURITY (IN THOUSANDS)**

	<u>Amortized Cost or Cost Value</u>	<u>Fair Value</u>
<b>DECEMBER 31, 2015</b>		
<b>Held-to-maturity securities:</b>		
Due in one year or less	\$ 1,156	\$ 1,169
Due in one year through five years	1,027	1,022
Due in five years or more	<u>1,834</u>	<u>1,770</u>
<b>Total held-to-maturity</b>	<b><u>\$ 4,017</u></b>	<b><u>\$ 3,961</u></b>

There were gross realized gains of \$46,000 and \$36,000 for the years ended December 31, 2015 and 2014, respectively, that were included in net investment income. There were gross realized losses of \$146,000 and \$2,000 for the year ended December 31, 2015 and 2014. 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, 2015, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was \$206,000 and the aggregate estimated fair value was \$2,070,000. For available-for-sale investments in an unrealized loss position at December 31, 2015, the aggregate amount of unrealized loss that had been in an unrealized loss position for more than twelve months was \$43,000 and the aggregate estimated fair value was \$5,097,000. For available-for-sale investments in an unrealized loss position at December 31, 2014, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was \$25,000 and the aggregate estimated fair value was \$227,000. For

available-for-sale investments in an unrealized loss position at December 31, 2014, the aggregate amount of unrealized loss that had been in an unrealized loss position for more than twelve months was \$20,000 and the aggregate estimated fair value was \$5,020,000.

For held-to-maturity investments in an unrealized loss position at December 31, 2015, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was \$114,000 and the aggregate estimated fair value was \$2,383,000. There were no held-to-maturity investments in an unrealized loss position for more than twelve months at December 31, 2015. For held-to-maturity investments in an unrealized loss position at December 31, 2014, the aggregate amount of unrealized loss that had been in an unrealized loss position for less than twelve months was \$1,000 and the aggregate estimated fair value was \$166,000. There were no held-to-maturity investments in an unrealized loss position for more than twelve months at December 31, 2014.

## 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.

The Company measures certain assets at fair value on a nonrecurring basis. These assets are recognized at fair value when they are deemed to be other-than-temporarily impaired. The Company recorded \$0 during the years ended December 31, 2015 and December 31, 2014, for other-than-temporary impairments on those assets required to be measured at fair value on a nonrecurring basis.

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

	Level 1	Level 2	Level 3	Total
<b>DECEMBER 31, 2015</b>				
<b>Available-for-sale securities:</b>				
Common stocks	\$ 4,017	\$ -	\$ -	\$ 4,017
Total common stocks	<u>4,017</u>	<u>\$ -</u>	<u>\$ -</u>	<u>4,017</u>
Mutual funds				
U.S. Treasury obligations	-	858	-	858
Commercial mortgage-backed securities	-	606	-	606
Asset-backed securities	-	1,665	-	1,665
Agency obligations	-	404	-	404
Corporate bonds	-	1,463	-	1,463
Registered investment company	50	-	-	50
Total mutual funds	<u>50</u>	<u>4,996</u>	<u>-</u>	<u>5,046</u>
<b>Total investments</b>	<b><u>\$ 4,067</u></b>	<b><u>\$ 4,996</u></b>	<b><u>\$ -</u></b>	<b><u>\$ 9,063</u></b>
<b>DECEMBER 31, 2014</b>				
<b>Available-for-sale securities:</b>				
Common stocks	\$ 1,109	\$ -	\$ -	\$ 1,109
Total common stocks	<u>1,109</u>	<u>\$ -</u>	<u>\$ -</u>	<u>1,109</u>
Mutual funds				
U.S. Treasury obligations	-	854	-	854
Commercial mortgage-backed securities	-	602	-	602
Asset-backed securities	-	1,657	-	1,657
Agency obligations	-	402	-	402
Corporate bonds	-	1,456	-	1,456
Registered investment company	50	-	-	50
Total mutual funds	<u>50</u>	<u>4,971</u>	<u>-</u>	<u>5,021</u>
<b>Total investments</b>	<b><u>\$ 1,159</u></b>	<b><u>\$ 4,971</u></b>	<b><u>\$ -</u></b>	<b><u>\$ 6,130</u></b>

#### 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 \$1,473,000 and \$1,627,000 at December 31, 2015 and 2014, respectively, which are included in net receivables and payables to the parent. The Company made payments to BCBSSC for income taxes of \$6,260,000 and \$3,101,000 during the years ended December 31, 2015 and 2014, respectively.

Unrealized losses on investments charged directly to equity have been reduced by deferred income tax benefit of \$61,000 for the year ended December 31, 2015. Unrealized gains credited directly to equity have been reduced by deferred income tax expense of \$20,000 for the year ended December 31, 2014.

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, and the dividends received deduction allowed for tax purposes. The temporary differences that give rise to deferred tax assets and liabilities are primarily related to accrued expenses, fixed assets, and prepaid expenses. There was no valuation allowance at December 31, 2015 and 2014.

#### RECOGNIZED PROVISION FOR INCOME TAXES (IN THOUSANDS)

	Year ended December 31,	
	2015	2014
Current	\$ 6,106	\$ 4,251
Deferred	(2)	(128)
<b>Total income taxes incurred</b>	<b>\$ 6,104</b>	<b>\$ 4,123</b>

#### DEFERRED TAX ASSETS & LIABILITIES (IN THOUSANDS)

	December 31,	
	2015	2014
<b>Deferred tax assets:</b>		
Current	\$ 2,826	\$ 3,055
Long-term	30	-
	<u>\$ 2,856</u>	<u>3,055</u>
<b>Deferred tax liabilities:</b>		
Current	\$ 117	\$ 261
Long-term	\$ 1,175	\$ 1,293
	<u>1,292</u>	<u>1,554</u>
<b>Net deferred tax asset</b>	<b>\$ 1,564</b>	<b>\$ 1,501</b>

#### **NOTE 5 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 \$53,780,000 and \$53,641,000 for the years ended December 31, 2015 and 2014, respectively. The Company paid \$66,406,000 and \$71,917,000 during the years ended December 31, 2015 and 2014, 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 \$10,827,000 and \$11,819,000 for these services during the years ended December 31, 2015 and 2014, 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 \$1,757,000 and \$1,618,000 for these services during the years ended December 31, 2015 and 2014, 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, 2015. 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, 2015. 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.

#### **NOTE 6 (CONTINUED)**

The Company recorded an estimated contingent liability for potential repayments of costs claimed on its contracts with CMS. The liability was \$5,300,000 and \$5,615,000 at December 31, 2015 and 2014, respectively.

The Company leases a building under an operating lease agreement which expires in 2016. Total rent expense under this operating lease was \$1,030,000 and \$1,781,000 for the years ended December 31, 2015 and 2014, 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 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 2015 and 2014. 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, 2015 and 2014.

The cost of providing the 401(k) contribution was \$2,440,000 and \$2,616,000 for the years ended December 31, 2015 and 2014, respectively. The pension expense allocated to the Company under the BCBSSC defined benefit pension plan was \$4,839,000 and \$4,780,000 for the years ended December 31, 2015 and 2014, respectively.

#### **NOTE 8 SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION**

Restricted cash and cash equivalents and restricted cash liability increased by \$204,000 in 2015 and \$234,000 in 2014.



