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Financial & Shareholder
Information

 **TRIPLE-S** MANAGEMENT

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Special Note Regarding Forward-Looking Statements

This Annual Report contains forward-looking statements, as such term is defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements are statements that include information about possible or assumed future sales, results of operations, developments, regulatory approvals or other circumstances. Statements that use the terms “believe”, “expect”, “plan”, “intend”, “estimate”, “anticipate”, “project”, “may”, “will”, “shall”, “should” and similar expressions, whether in the positive or negative, are intended to identify forward-looking statements.

All forward-looking statements in this Annual Report reflect our current views about future events and are based on assumptions and subject to risks and uncertainties. Consequently, actual results may differ materially from those anticipated in these forward-looking statements as a result of various factors.

In addition, we operate in a highly competitive, constantly changing environment that is significantly influenced by very large organizations that have resulted from business combinations, aggressive marketing and pricing practices of competitors and regulatory oversight. The following list is a summary of factors, the results of which, either individually or in combination, if markedly different from our planning assumptions, could cause our business results of operations, financial condition, cash flow, or prospect, to be materially adversely affected from those expressed in any forward-looking statements contained in this Annual Report:

- trends in health care costs and utilization rates;
- ability to secure sufficient premium rate increases;
- competitor pricing below market trends of increasing costs;
- re-estimates of our policy and contract liabilities;
- changes in government regulation of managed care, life insurance or property and casualty insurance;
- significant acquisitions or divestitures by major competitors;
- introduction and use of new prescription drugs and technologies;
- a downgrade in our financial strength ratings;
- litigation or legislation targeted at managed care, life insurance or property and casualty insurance companies;
- ability to contract with providers and government agencies consistent with past practice;
- ability to successfully implement our disease management and utilization management programs;
- volatility in the securities markets and investment losses and defaults; and
- general economic downturns, major disasters and epidemics.

The foregoing list should not be construed to be exhaustive. We believe the forward-looking statements in this Annual Report are reasonable; however, there is no assurance that the actions, events or results anticipated by the forward-looking statements will occur or, if any of them do, what impact they will have on our results of operations or financial condition. In view of these uncertainties, you should not place undue reliance on any forward-looking statements, which are based on our current expectations at the time the statements are made. Further, forward-looking statements speak only as of the date they are made, and, other than as required by applicable law, including the securities laws of the United States, we do not intend to update or revise any of them in light of new information or future events.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

This financial discussion contains an analysis of our consolidated financial position and financial performance as of December 31, 2018 and 2017, and consolidated results of operations for 2018, 2017 and 2016. References to the terms "we", "our" or "us" used throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), refer to TSM and unless the context otherwise requires, its direct and indirect subsidiaries. This analysis should be read in its entirety and in conjunction with the consolidated financial statements, notes and tables included elsewhere in this Annual Report on Form 10-K.

Overview

We are one of the most significant players in the managed care industry in Puerto Rico and have 60 years of experience in this industry. We offer a broad portfolio of managed care and related products in the Commercial, Medicare, and the Government of Puerto Rico health insurance plan (similar to Medicaid) ("Medicaid" or "the Government health plan") markets. In the Commercial market we offer products to corporate accounts, U.S. federal government employees, local government employees, individual accounts and Medicare Supplement. We market our managed care products through an extensive network of independent agents and brokers located throughout Puerto Rico, as well as an internal salaried sales force. Medicaid is funded by the Government of Puerto Rico and the U.S. Government.

We have the exclusive right to use the BCBS name and mark throughout Puerto Rico, the U.S. Virgin Islands, Costa Rica, the British Virgin Islands and Anguilla. As of December 31, 2018 we serve approximately 876,000 members across all regions of Puerto Rico. For the years ended December 31, 2018 and 2017 respectively, our Managed Care segment represented approximately 92% of our total consolidated premiums earned, net. We also participate in the life and property and casualty insurance markets in Puerto Rico.

We participate in the managed care market through our subsidiaries, TSS, TSB and TSA. TSS, TSA, and TSB are BCBSA licensees.

We participate in the life insurance market through our subsidiary, TSV, and in the property and casualty insurance market through our subsidiary, TSP.

The Commissioner of Insurance of the Government of Puerto recognizes only statutory accounting practices for determining and reporting the financial condition and results of operations of an insurance company, for determining its solvency under the Puerto Rico insurance laws, and for determining whether its financial condition warrants the payment of a dividend to its stockholders. No consideration is given by the Commissioner of Insurance of Puerto Rico to financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") in making such determinations. See Note 25, *Statutory Accounting*, of the Notes to Consolidated Financial Statements, included in this Annual Report.

2018 Consolidated Highlights

Key developments in our business during 2018 are described below:

- Consolidated premiums earned, net increased 4.0% year over year, to \$2.9 billion, primarily reflecting higher Managed Care premiums;
- Managed Care premiums increased 3.8% when compared to last year, primarily reflecting growth in Medicare premiums following the Company's achievement of a four-star rated Medicare Advantage HMO contract this year, resulting in a 5% bonus applied to the benchmark used in the premium calculation, as well as an increase in the 2018 Medicare reimbursement rates. This increase was partially offset by lower membership.
- Consolidated claims for the year were \$2.5 billion, up 7.4% over last year, primarily reflecting the \$128.7 million unfavorable prior period reserve development in the Property and Casualty segment related to Hurricane Maria losses. Hurricane Maria was a category 4 hurricane that impacted Puerto Rico in September 2017. In addition, in 2017 the Managed Care segment experienced significantly

lower utilization in the aftermath of Hurricanes Irma and Maria. The consolidated loss ratio was up 280 basis points, to 86.0%, and the MLR decreased 110 basis points, to 84.5%.

- Consolidated operating expenses for the year were \$554.7 million and the operating expense ratio was 18.8%.
- Net loss for the year was \$63.3 million, a decrease from a net income of \$54.5 million for the prior year, primarily reflecting the unfavorable prior period reserve development in the Property and Casualty segment related to the aforementioned hurricanes, the lower Managed Care utilization experienced in 2017 due to the aftermath of the hurricanes, and the impact of the net unrealized losses on equity investments. The unrealized loss on equity investments is due to the implementation effective January 1, 2018 of new accounting guidance that requires the change in unrealized gain (loss) of equity investments, previously recognized through comprehensive income, to be recorded through earnings.

Overview details

Intersegment revenues and expenses are reported on a gross basis in each of the operating segments but eliminated in the consolidated results. Except as otherwise indicated, the numbers presented in this Annual Report on Form 10-K do not reflect intersegment eliminations. These intersegment revenues and expenses affect the amounts reported on the financial statement line items for each segment, but are eliminated in consolidation and do not change net income. The following table shows premiums earned, net and net fee revenue and operating income for each segment, as well as the intersegment premiums earned, service revenues and other intersegment transactions, which are eliminated in the consolidated results:

<i>(Dollar amounts in millions)</i>	Years ended December 31,		
	2018	2017	2016
Premiums earned, net:			
Managed care	\$2,689.1	\$2,590.0	\$2,648.5
Life insurance	168.6	161.8	156.9
Property and casualty insurance	83.5	77.2	87.9
Intersegment premiums earned	(2.6)	(2.1)	(2.7)
Consolidated premiums earned, net	\$2,938.6	\$2,826.9	\$2,890.6
Administrative service fees:			
Managed care	\$ 19.1	\$ 21.6	\$ 22.4
Intersegment administrative service fees	(4.4)	(5.1)	(4.5)
Consolidated administrative service fees	\$ 14.7	\$ 16.5	\$ 17.9
Operating income (loss):			
Managed care	\$ 26.5	\$ 55.0	\$ (36.8)
Life insurance	19.9	19.4	21.5
Property and casualty insurance	(110.1)	(6.0)	12.1
Intersegment and other	2.0	-	(2.0)
Consolidated operating (loss) income	\$ (61.3)	\$ 68.4	\$ (5.2)

Revenue

General. Our revenue consists primarily of (i) premium revenue generated from our Managed Care segment, (ii) administrative service fees received for services provided to self-insured employers, (iii) premiums we generate from our Life and Property and Casualty segments, and (iv) investment income.

Premium Revenue. Our revenue primarily consists of premiums earned from the sale of managed care products to the Commercial, Medicare Advantage and Medicaid sectors. We receive a monthly payment from or on behalf of each member enrolled in our managed care plans (excluding ASO). We recognize all premium revenue in our Managed Care segment during the month in which we are obligated to provide services to an enrolled member. Premiums we receive in advance of that date are recorded as unearned premiums.

Premiums are set prospectively, meaning that a fixed premium rate is determined at the beginning of each contract year and revised at renewal. We renegotiate the premiums of different groups as their existing annual contracts become due. Our Medicare Advantage contracts entitle us to premium payments from CMS on behalf of each Medicare beneficiary enrolled in our plans, generally on a per member per month ("PMPM") basis. We submit rate proposals to CMS in June for each Medicare Advantage product that will be offered beginning January 1 of the subsequent year in accordance with the competitive bidding process under the MMA. Retroactive rate adjustments are made periodically with respect to our Medicare Advantage plans based on the aggregate health status and risk scores of our plan participants. Premium rates for the Medicaid business are based on a bid contract with ASES and are revised each year, at which time rates are fixed for the plan year.

Premiums on traditional life insurance policies are reported as earned when due. Premiums on accident and health and other short-term contracts are recognized as earned, primarily on a pro rata basis over the contract period. Premiums on credit life policies are recognized as earned in proportion to the amounts of insurance in force. Group insurance premiums are billed one month in advance and a grace period of one month is provided for premium payment. If the insured fails to pay within the one-month grace period, we may cancel the policy. We recognize premiums on property and casualty contracts as earned on a pro rata basis over the policy term. Property and casualty policies are subscribed through general agencies, which bill policy premiums to their clients in advance or, in the case of new business, at the inception date and remit collections to us, net of commissions. The portion of premiums related to the period prior to the end of coverage is recorded in the consolidated balance sheet as unearned premiums and is transferred to premium revenue as earned.

Administrative Service Fees. Administrative service fees include amounts paid to us for administrative services provided to self-insured contracts. We provide a range of customer services pursuant to our administrative services only ("ASO") contracts, including claims administration, billing, access to our provider networks and membership services. Administrative service fees are recognized in the month in which services are provided.

Investment Income. Investment income consists of interest and dividend income from investment securities. See Note 5, *Net Investment Income*, of the Notes to Consolidated Financial Statements, included in this Annual Report.

Expenses

Claims Incurred. Our largest expense is the Managed Care segment's medical claims incurred, or the cost of medical services we arrange for our members. Medical claims incurred include the payment of benefits and losses, mostly to physicians, hospitals, pharmacies, and other service providers, and to policyholders. We generally pay our providers on one of three forms: (1) fee-for-service contracts based on negotiated fee schedules; (2) capitation arrangements, generally on a fixed PMPM payment basis, whereby the provider generally assumes some of the medical expense risk; and (3) risk-sharing arrangements, whereby we advance a PMPM payment and share the risk of certain medical costs of our members with the provider based on actual experience as measured against pre-determined sharing ratios. Claims incurred also include claims incurred in our Life and Property and Casualty segments. Each segment's results of operations depend to a significant extent on our ability to accurately predict and effectively manage claims and losses. A portion of the claims incurred for each period consists of claims

reported but not paid during the period, as well as a management and actuarial estimate of claims incurred but not reported during the period.

The MLR, which is calculated by dividing managed care claims incurred by managed care premiums earned, net is one of our primary management tools for measuring these costs and their impact on our profitability. The MLR is affected by the cost and utilization of services. The cost of services is affected by many factors, in particular our ability to negotiate competitive rates with our providers. The cost of services is also influenced by inflation and new medical discoveries, including new prescription drugs, therapies and diagnostic procedures. Utilization rates, which reflect the extent to which beneficiaries utilize healthcare services, significantly influence our medical costs. The level of utilization of services depends in large part on the age, health and lifestyle of our members, among other factors. As the MLR is the ratio of claims incurred to premiums earned, net, it is affected not only by our ability to contain cost trends but also by our ability to increase premium rates to levels consistent with or above medical cost trends. We use MLRs both to monitor our management of healthcare costs and to make various business decisions, including what plans or benefits to offer and our selection of healthcare providers.

Operating Expenses. Operating expenses include commissions to external brokers, general and administrative expenses, cost containment expenses such as case and disease management programs, and depreciation and amortization. The operating expense ratio is calculated by dividing operating expenses by premiums earned, net plus administrative service fees. A significant portion of our operating expenses are fixed costs. Accordingly, it is important that we maintain certain level of volume of business in order to compensate for the fixed costs. Significant changes in our volume of business will affect our operating expense ratio and results of operations. We also have variable costs, which vary in proportion to changes in volume of business.

Membership

Our results of operations depend in large part on our ability to maintain or grow our membership. In addition to driving revenues, membership growth is necessary to successfully introduce new products, maintain an extensive network of providers and achieve economies of scale. Our ability to maintain or grow our membership is affected principally by the competitive environment, the economy, and general market conditions.

The following table sets forth selected membership data as of the dates set forth below:

	As of December 31,		
	2018	2017	2016
Commercial ⁽¹⁾	449,047	475,026	509,157
Medicare	108,605	118,451	110,297
Medicaid	318,616	384,462	397,918
Total	876,268	977,939	1,017,372

(1) Commercial membership includes corporate accounts, self-funded employers, individual accounts, Medicare Supplement, federal government employees and local government employees.

Results of Operations

Consolidated Operating Results

The following table sets forth our consolidated operating results for the years ended December 31, 2018, 2017 and 2016. Further details of the results of operations of each reportable segment are included in the analysis of operating results for the respective segments.

<i>(Dollar amounts in millions)</i>	2018	2017	2016
<i>Years ended December 31,</i>			
Revenues:			
Premiums earned, net	\$ 2,938.6	\$ 2,826.9	\$ 2,890.6
Administrative service fees	14.7	16.5	17.9
Net investment income	61.9	51.6	48.9
Other operating revenues	5.8	3.7	3.5
Total operating revenues	3,021.0	2,898.7	2,960.9
Net realized investment gains	0.3	10.8	17.4
Net unrealized investment losses on equity investments	(36.5)	-	-
Other income, net	11.3	6.6	6.5
Total revenues	2,996.1	2,916.1	2,984.8
Benefits and expenses:			
Claims incurred	2,527.6	2,353.1	2,472.2
Operating expenses	554.7	477.2	493.9
Total operating costs	3,082.3	2,830.3	2,966.1
Interest expense	6.9	6.8	7.6
Total benefits and expenses	3,089.2	2,837.1	2,973.7
(Loss) income before taxes	(93.1)	79.0	11.1
Income (benefit) tax expense	(29.8)	24.5	(6.3)
Net (loss) income	(63.3)	54.5	17.4
Net loss attributable to non-controlling interest	-	-	-
Net (loss) income attributable to TSM	\$ (63.3)	\$ 54.5	\$ 17.4

Year ended December 31, 2018 compared with the year ended December 31, 2017

Operating Revenues

Premiums earned, net increased by \$111.7 million, or 4.0%, to \$2.9 billion. This increase primarily reflects higher premiums in the Managed Care segment by \$99.1 million. Most of the growth in managed care premiums was experienced in the Medicare business, reflecting the achievement of a four-star rated Medicare Advantage HMO contract this year, resulting in a 5% bonus applied to the benchmark used in the premium calculation, as well as an increase in the 2018 Medicare reimbursement rates. This increase was partially offset by lower managed care membership.

Administrative service fees decreased \$1.8 million, or 10.9%, mainly due to lower membership enrolled in this business.

Net investment income increased \$10.3 million, or 20.0%, to \$61.9 million as a result of higher invested balances and interest rates.

Net unrealized investment losses on equity investments

The \$36.5 million in consolidated net unrealized investment losses on equity investments reflects the impact of new accounting guidance implemented effective January 1, 2018, which requires the change in unrealized gain (loss) of equity investments, previously recorded through comprehensive income, to be recorded through earnings.

Claims Incurred

Consolidated claims incurred increased by \$174.5 million, or 7.4%, to \$2.5 billion, mostly driven by an increase in the Property and Casualty segment gross losses related to Hurricane Maria, a category 4 hurricane that impacted Puerto Rico in September 2017, causing the segment to exceed its applicable catastrophe reinsurance coverage limits and resulting in \$128.7 million unfavorable reserve development recorded in 2018. In addition, in 2017 the Managed Care segment experienced significantly lower utilization following the hurricanes that occurred during that year, this hurricane-related drop in utilization is estimated to have lowered the Managed Care segment's claims by approximately \$55 million. The 2017 period also includes \$14.8 million of losses related to Hurricanes Irma and Maria recognized by the Property and Casualty segment. The consolidated loss ratio increased by 280 basis points to 86.0%.

Operating Expenses

Consolidated operating expenses increased by \$77.5 million, or 16.2%, to \$554.7 million. The higher operating expenses are mostly the result of the reinstatement of the HIP Fee of \$50.1 million and higher professional services and personnel costs related to the ongoing managed care initiatives. The consolidated expense ratio increased 200 basis points to 18.8%.

Income taxes

Consolidated income tax benefit for the year ended December 31, 2018 was \$29.8 million, compared to an expense of \$24.5 million during the last year, primarily due to a change in the effective tax rate of certain deferred tax liabilities in the Company's Property and Casualty segment in order to reflect the expected tax rate at which they will reverse, and a change in the enacted tax rate, from 39% to 37.5%, following the Puerto Rico income tax reform enacted in December 2018. These changes increased the deferred tax expense by approximately \$9.5 million. The consolidated income tax expense also reflects the tax impact of net unrealized losses on equity investments and the lower operating income of the Managed Care segment.

Year ended December 31, 2017 compared with the year ended December 31, 2016

Operating Revenues

Premiums earned, net decreased by \$63.7 million, or 2.2%, to \$2.8 billion. This decrease primarily reflects lower premiums in the Managed Care segment by \$58.5 million mainly due to lower membership in the segment's Medicaid and Commercial businesses, the impact of the suspension of the HIP fee pass through, and lower Medicare additional risk score revenue. These decreases were partially offset by higher average premium rates in the Commercial and Medicaid businesses as well as by higher Medicare membership. Property and casualty premiums decreased by \$10.7 million year over year, mostly reflecting the \$9.2 million estimated catastrophe reinsurance reinstatement costs following the impact of Hurricanes Irma and Maria in September 2017.

Administrative service fees decreased \$1.4 million, or 7.8%, mainly due to lower membership enrolled in this business.

Net investment income increased \$2.7 million, or 5.5%, to \$51.6 million mostly as a result of higher invested balances.

Claims Incurred

Consolidated claims incurred decreased by \$119.1 million, or 4.8%, to \$2.4 billion, mostly due to lower claims in the Managed Care segment offset by an increase in claims in the Property and Casualty segment. The decrease in managed care claims primarily reflects lower claims incurred across all businesses in the segment driven by the estimated decrease in utilization as a consequence of the aforementioned hurricanes, lower enrollment in the Commercial and Medicaid enrollment, and favorable fluctuations in the prior period reserve developments in the Commercial and Medicare businesses. The Property and Casualty segment's estimated net retained losses related to Hurricanes Irma and Maria were approximately \$14.8 million after the application of reinsurance. The consolidated loss ratio decreased by 230 basis points to 83.2%. Excluding the impact of prior-period reserve developments, and moving the Medicare risk score revenue and other revenue adjustments to the corresponding period, the managed care MLR for the year was 83.7%, 100 basis points lower than the same metric from the prior year.

Operating Expenses

Consolidated operating expenses decreased by \$16.7 million, or 3.4%, to \$477.2 million. The lower operating expenses are mostly the result of the decrease in the HIP Fee of \$44.2 million due to the 2017 moratorium offset by increase in personnel costs, professional services, and business promotion expenses totaling approximately \$30.4 million.

Income taxes

Consolidated income taxes increased by \$30.8 million, to a net expense of \$24.5 million. The year over year change in income taxes primarily results from an increase in the taxable income from the Managed Care segment, which has a higher effective tax rate than our other segments.

Managed Care Segment Operating Results

We offer our products in the Managed Care segment to three distinct market sectors in Puerto Rico: Commercial, Medicare Advantage and Medicaid. For the year ended December 31, 2018, the Commercial, Medicare and Medicaid sectors represented 26.6%, 38.5% and 26.4% of our consolidated premiums earned, net, respectively.

<i>(Dollar amounts in millions)</i>	2018	2017	2016
Operating revenues:			
Medical premiums earned, net:			
Commercial	\$ 782.8	\$ 803.3	\$ 841.4
Medicare	1,130.3	1,035.3	1,023.9
Medicaid	776.0	751.4	783.2
Medical premiums earned, net	2,689.1	2,590.0	2,648.5
Administrative service fees	19.1	21.6	22.4
Net investment income	23.8	16.6	15.1
Total operating revenues	2,732.0	2,628.2	2,686.0
Medical operating costs:			
Medical claims incurred	2,272.5	2,218.3	2,347.5
Medical operating expenses	433.0	354.9	375.3
Total medical operating costs	2,705.5	2,573.2	2,722.8
Medical operating income (loss)	\$ 26.5	\$ 55.0	\$ (36.8)
Additional data:			
Member months enrollment:			
Commercial:			
Fully-insured	3,775,441	3,981,347	4,209,920
Self-funded	1,732,219	1,967,668	2,144,621
Total Commercial member months	5,507,660	5,949,015	6,354,541
Medicare member months	1,337,061	1,457,363	1,394,272
Medicaid member months	4,555,702	4,631,316	4,829,729
Total member months	11,400,423	12,037,694	12,578,542
Medical loss ratio	84.5%	85.6%	88.6%
Operating expense ratio	16.0%	13.6%	14.1%

Year ended December 31, 2018 compared with the year ended December 31, 2017

Medical Operating Revenues

Medical premiums earned increased by \$99.1 million, or 3.8%, to \$2.7 billion. This increase is principally the result of the following:

- Medical premiums generated by the Commercial business decreased by \$20.5 million, or 2.6%, to \$782.8 million. This fluctuation primarily reflects lower fully-insured enrollment during the year of approximately 206,000 member months offset in part by \$12.1 million related to the reinstatement of the HIP fee pass-through in 2018 and higher average premium rates.
- Medical premiums generated by the Medicare business increased by \$95.0 million, or 9.2%, to \$1,130.3 million, primarily reflecting an increase in the 2018 Medicare reimbursement rates fee-for-service benchmark for the first time since 2012, an increase in rates as the result of attaining a four-star rating in the Company's 2018 HMO product, and higher average membership risk score. These increases were partially offset by lower enrollment of approximately 120,000 member months.

- Medical premiums generated by the Medicaid business increased by \$24.6 million, or 3.3%, to \$776.0 million. This increase primarily reflects higher premiums rates effective July 1, 2017 and \$14.5 million related to the reinstatement of the HIP fee pass-through. These increases were offset in part by a lower enrollment by approximately 76,000 in member months and the impact of the profit sharing accrual, which lowered 2018 premiums by \$4.3 million. The lower membership reflects the lower membership assigned by ASES when implementing the current Medicaid contract, which was effective November 1, 2018. At the effective date of the current agreement TSS was assigned by ASES approximately 280,000 subscribers. After this date, subscribers had approximately three months to select their insurance carrier, during which time TSS was able to compete for membership across Puerto Rico. As of December 31, 2018, our Medicaid membership was approximately 319,000 members.

Medical Claims Incurred

Medical claims incurred increased by \$54.2 million, or 2.4%, to \$2.3 billion. The MLR of the segment decreased 110 basis points during the 2018 period, to 84.5%. These fluctuations are primarily attributed to the net effect of the following:

- The medical claims incurred of the Commercial business increased by \$22.3 million, or 3.6%, during the 2018 period and its MLR, at 82.4%, was 490 basis points higher than the same period last year primarily reflecting the decrease in utilization in the 2017 period caused by Hurricanes Irma and Maria. The hurricane related decrease in utilization was estimated to lower 2017 claims by approximately \$27.8 million, or 340 basis points of last year's MLR. Adjusting for the effect of prior period reserve development in 2018 and 2017 period as well as adjusting for the 2017 hurricane related impact in utilization, the Commercial MLR would have been approximately 83.4%, 330 basis points higher than last year, reflecting claim trends higher than premium trends.
- The medical claims incurred of the Medicare business increased by \$33.1 million, or 3.6%, during the 2018 period and its MLR decreased by 450 basis points, to 83.2%. The hurricane related decrease in utilization was estimated to lower 2017 claims by approximately \$25.1 million, or 240 basis points of last year's MLR. Adjusting for the effect of prior period reserve development in the 2018 and 2017 periods, moving the risk score revenue to its corresponding period, as well as adjusting for the 2017 hurricane related impact in utilization, the Medicare MLR would have been approximately 83.9%, 640 basis points lower than last year, primarily reflecting the higher premium rates in the 2018 period as well as cost containment initiatives implemented during the year.
- The medical claims incurred of the Medicaid business decreased by \$1.1 million, or 0.2%, during the 2018 period and its MLR decreased by 300 basis points, to 88.5%. The hurricane related decrease in utilization was estimated to lower 2017 claims by approximately \$2.2 million, or 30 basis points of last year's MLR. Adjusting for the effect of prior period reserve developments and the 2018 profit sharing accrual, the Medicaid MLR would have been approximately 87.8%, 420 basis points lower than the adjusted MLR for last year mostly reflecting the impact of higher premium rates in 2018 and cost containment initiatives.

Medical Operating Expenses

Medical operating expenses increased by \$78.1 million, or 22.0%, to \$433.0 million. The operating expense ratio increased by 240 basis points to 16.0% in 2018. The higher operating expenses and expense ratio are mostly driven by the reinstatement of the HIP fee in 2018, resulting in an increase of \$50.1 million, and professional services and personnel costs related to ongoing operational and clinical initiatives.

Year ended December 31, 2017 compared with the year ended December 31, 2016

Medical Operating Revenues

Medical premiums earned decreased by \$58.5 million, or 2.2%, to \$2.6 billion. This decrease is principally the result of the following:

- Medical premiums generated by the Commercial business decreased by \$38.1 million, or 4.5%, to \$803.3 million. This fluctuation primarily reflects lower fully-insured enrollment during the year of approximately 228,600 member months and \$14.5 million related to the suspension of the HIP fee pass-through; offset by an increase in average premium rates of approximately 5%.
- Medical premiums generated by the Medicare business increased by \$11.4 million, or 1.1%, to \$1,035.3 million, primarily reflecting an increase in member months enrollment of approximately 63,100 lives. This increase is partially offset by lower additional risk score revenue by \$30.9 million as well as lower average premium rates due to a reduction in the 2017 Medicare reimbursement rates.
- Medical premiums generated by the Medicaid business decreased by \$31.8 million to \$751.4 million. This decrease primarily reflects lower fully-insured member months enrollment by approximately 198,400 lives, \$10.8 million related to the suspension of the HIP fee pass-through as a result of the 2017 moratorium and, the impact of the 2.5% excess profit accrual that increased 2016 premiums by \$10.9 million. Decreases are partially offset by a \$12.2 million increase in premium collections related to our compliance with the contract's quality incentive metrics and the impact of the new premium rates that were effective July 1, 2017, which increased average premium rates by approximately 9%.

Medical Claims Incurred

Medical claims incurred decreased by \$129.2 million, or 5.5%, to \$2.2 billion. The MLR of the segment decreased 300 basis points during the 2017 period, to 85.6%. These fluctuations are primarily attributed to the net effect of the following:

- The medical claims incurred of the Commercial business decreased by \$94.5 million, or 13.2%, during the 2017 period and its MLR, at 77.5%, was 770 basis points lower than the same period last year. Adjusting for the effect of prior period reserve developments, the Commercial MLR would have been 77.9%, 590 basis points lower than the adjusted MLR for last year, primarily reflecting the estimated decrease in utilization caused by Hurricanes Irma and Maria in September 2017 as well as the ongoing claim trends that are lower than our premium trends following the continuity of our underwriting discipline. The estimated decrease in utilization related to the aforementioned hurricanes account for approximately 340 of the 590 basis-points decrease in the adjusted MLR.
- The medical claims incurred of the Medicare business decreased by \$16.6 million, or 1.8%, during the 2017 period and its MLR decreased by 260 basis points, to 87.7%. Adjusting for the effect of prior period reserve developments in 2017 and 2016 and moving the additional risk score revenue adjustments to their corresponding period, the Medicare MLR would have been approximately 88.4%, about 80 basis points lower than last year. The estimated decrease in utilization caused by Hurricanes Irma and Maria mitigated the impact of the higher trends in Part B drugs and pharmacy benefits experienced by this business as well as the improvement of benefits in 2017 products taking advantage of the HIP fee moratorium. The estimated decrease in utilization related to the aforementioned hurricanes lowered by approximately 240 basis points the adjusted MLR.
- The medical claims incurred of the Medicaid business decreased by \$18.2 million, or 2.6%, during the 2017 period and its MLR increased by 140 basis points, to 91.5%. Adjusting for the effect of prior period reserve developments in 2017 and 2016, as well as for the impact of the 2.5% excess profit accrual and this year's quality incentive premiums, the Medicaid MLR would have been approximately 91.8%, about 180 basis points higher than last year. The higher MLR primarily reflects increased pharmacy and outpatient claim trends, partially offset by the estimated decrease in utilization caused by Hurricanes Irma and Maria, which lowered the adjusted MLR by 30 basis points, and the impact of the higher premium rates that were effective July 1, 2017.

Medical Operating Expenses

Medical operating expenses decreased by \$20.4 million, or 5.4%, to \$354.9 million. The operating expense ratio decreased by 50 basis points to 13.6% in 2017. The lower operating expenses and expense ratio are mostly the result of the decrease in the HIP Fee of \$44.2 million due to the 2017 moratorium offset by increase in personnel costs, professional services and business promotion expenses totaling approximately \$28.1 million.

Life Segment Operating Results

<i>(Dollar amounts in millions)</i>	2018	2017	2016
<i>Years ended December 31,</i>			
Operating revenues:			
Premiums earned, net:			
Premiums earned	\$ 175.3	\$ 166.4	\$ 161.3
Assumed earned premiums	2.1	4.2	4.4
Ceded premiums earned	(8.8)	(8.8)	(8.8)
Premiums earned, net	168.6	161.8	156.9
Net investment income	25.6	24.8	24.9
Total operating revenues	194.2	186.6	181.8
Operating costs:			
Policy benefits and claims incurred	99.0	87.3	86.9
Underwriting and other expenses	75.3	79.9	73.4
Total operating costs	174.3	167.2	160.3
Operating income	\$ 19.9	\$ 19.4	\$ 21.5
Additional data:			
Loss ratio	58.7%	54.0%	55.4%
Expense ratio	44.7%	49.4%	46.8%

Year ended December 31, 2018 compared with the year ended December 31, 2017

Operating Revenues

Premiums earned, net increased by \$6.8 million, or 4.2% to \$168.6 million, mainly as the result of higher sales and improved policy retention in the Individual Life and Cancer lines of business.

Policy Benefits and Claims Incurred

Policy benefits and claims incurred increased by \$11.7 million, or 13.4%, to \$99.0 million, mostly resulting from higher number of deaths benefits paid in the Individual Life line of business, an increased average cost of claims in the Cancer line of business, and higher actuarial reserves following improved portfolio persistency. The segment's loss ratio increased 470 basis points, to 58.7%.

Underwriting and Other Expenses

Decrease in underwriting and other expenses of \$4.6 million, or 5.8%, to \$75.3 million mostly results from a lower amortization of deferred acquisition costs and value of business acquired assets reflecting the segment's improved portfolio persistency. As a result, the segment's operating expense ratio improved to 44.7%, or 470 basis points.

Year ended December 31, 2017 compared with the year ended December 31, 2016

Operating Revenues

Premiums earned, net increased by \$4.9 million, or 3.1% to \$161.8 million, as the result of premium growth in the segment's Individual Life and Cancer lines of business, as well as growth in the Costa Rica operations.

Policy Benefits and Claims Incurred

Policy benefits and claims incurred increased by \$0.4 million, or 0.5%, to \$87.3 million, mostly reflecting a higher volume of business during the year, particularly in the Cancer and Individual Life lines of business, which claims increased by \$2.7 million, offset by a decrease of \$2.3 million in actuarial reserves.

Underwriting and Other Expenses

Increase in underwriting and other expenses of \$6.5 million, or 8.9%, to \$79.9 million mostly reflects higher commissions following the segment's premium growth mentioned above. In addition, the segment has incurred in higher development and marketing expenses related to the expansion of the Costa Rica operations. As a result, the segment's operating expense ratio increased to 49.4%, or 260 basis points.

Property and Casualty Segment Operating Results

<i>(Dollar amounts in millions)</i>	2018	2017	2016
<i>Years ended December 31,</i>			
Operating revenues:			
Premiums earned, net:			
Premiums written	\$ 139.8	\$ 143.8	\$ 133.1
Premiums ceded	(60.4)	(62.3)	(46.0)
Change in unearned premiums	4.1	(4.3)	0.8
Premiums earned, net	83.5	77.2	87.9
Net investment income	10.8	9.5	8.9
Total operating revenues	94.3	86.7	96.8
Operating costs:			
Claims incurred	159.9	50.8	40.8
Underwriting and other operating expenses	44.5	41.9	43.9
Total operating costs	204.4	92.7	84.7
Operating (loss) income	\$ (110.1)	\$ (6.0)	\$ 12.1
Additional data:			
Loss ratio	191.5%	65.8%	46.4%
Expense ratio	53.3%	54.3%	49.9%

Year ended December 31, 2018 compared with the year ended December 31, 2017

Operating Revenues

Total premiums written decreased by \$4.0 million, or 2.8%, to \$139.8 million, driven by lower sales of Commercial Package products, mostly the result of selective and disciplined underwriting of Commercial risks.

The premiums ceded to reinsurers decreased by \$1.9 million, or 3.0%. Prior year premiums ceded include approximately \$9.2 million of catastrophe reinsurance reinstatement costs. The 2018 includes an increase in cessions in the Commercial quota share agreement from 30% in 2017 to 35% effective April 2018, as well as higher reinsurance costs for facultative and nonproportional property reinsurance.

The \$8.4 million increase in the change in unearned premiums reflects the segments lower premiums written in 2018.

Claims Incurred

Claims incurred increased by \$109.1 million, or 214.8%, to \$159.9 million mostly driven by an increase in gross losses related to Hurricane Maria, causing the segment to exceed the applicable catastrophe reinsurance coverage limits and resulting in a \$128.7 million unfavorable reserve development. As loss information emerged, reserves have been updated to reflect a worsening in the loss expectations for Hurricane Maria. As a result, the segment's loss ratio increased to 191.5% during this period. In 2017 we recognized \$14.8 million of hurricane related net losses.

Underwriting and Other Expenses

Underwriting and other operating expenses increased by \$2.6 million, or 6.2%, to \$44.5 million mostly due to higher acquisition expenses, professional services, and personnel costs. The operating expense ratio decreased by 100 basis points, to 53.3% in 2018.

Year ended December 31, 2017 compared with the year ended December 31, 2016

Operating Revenues

Total premiums written increased by \$10.7 million, or 8.0%, to \$143.8 million, driven by higher sales of Commercial Property and Commercial Liability products, mainly as a result of the acquisition of a large account, as well as to higher sales of Personal package products.

The premiums ceded to reinsurers increased by \$16.3 million, or 35.4%, mostly reflecting higher premiums written in Commercial products during 2017 as well as adjustments related to the catastrophe reinsurance, including \$9.2 million for catastrophe reinsurance reinstatement costs.

The change in unearned premiums mostly reflects the segments higher premiums written in 2017.

Claims Incurred

Claims incurred increased by \$10.0 million, or 24.5%, to \$50.8 million mostly driven by \$14.8 million of net losses related to Hurricanes Irma and Maria. As a result, the segment's loss ratio increased by 1,940 basis points, to 65.8% during this period.

Underwriting and Other Expenses

Underwriting and other operating expenses decreased by \$2.0 million, or 4.6%, to \$41.9 million mostly due to lower personnel costs and net commissions. The operating expense ratio increased by 440 basis points, to 54.3% in 2017.

Liquidity and Capital Resources

Cash Flows

A summary of our major sources and uses of cash for the periods indicated is presented in the following table:

(Dollar amounts in millions)

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Sources (uses) of cash:			
Cash provided by operating activities	\$ 7.5	\$ 288.9	\$ 6.5
Net purchases of investment securities	(12.6)	(154.6)	(80.9)
Net capital expenditures	(19.8)	(21.4)	(4.8)
Proceeds from long-term borrowings	-	24.3	-
Payments of long-term borrowings	(3.2)	(27.1)	(1.7)
Proceeds from policyholder deposits	18.5	13.6	18.2
Surrenders of policyholder deposits	(26.7)	(22.1)	(21.9)
Repurchase and retirement of common stock	(22.4)	(20.2)	(21.4)
Other	(22.7)	14.1	11.6
Net (decrease) increase in cash and cash equivalents	<u>\$ (81.4)</u>	<u>\$ 95.5</u>	<u>\$ (94.4)</u>

Year ended December 31, 2018 compared to year ended December 31, 2017

Cash flow from operating activities decreased by \$281.4 million for the year ended December 31, 2018 as compared to the year ended December 31, 2017, mostly reflecting Property and Casualty hurricane related claim payments, last year's collection of advances from reinsurers, and the 2018 HIP Fee payment; offset in part by higher premium collections.

Decrease in net purchases of investments in securities are part of our asset/liability management strategy using cash on hand.

In August 2017, the Company's Board of Directors authorized a \$30.0 million repurchase program of its Class B common stock (2017 Repurchase Program) and in February 2018 the Company's Board of Directors authorized a \$25.0 million expansion of this program. Repurchases were conducted through open-market purchases of Class B shares only, in accordance with Rule 10b-18 under the Securities Exchange Act of 1934, as amended. During the year 2018, the Company repurchased and retired 903,888 shares of our Class B Common Stock shares at an average per share price of \$24.76, for an aggregate cost of \$22.4 million.

Increase in Other is due to the change in outstanding checks in excess of bank balances.

Year ended December 31, 2017 compared to year ended December 31, 2016

Cash flow from operating activities increased by \$279.7 million for the year ended December 31, 2017 as compared to the year ended December 31, 2016, principally due to, lower claims paid, a decrease in cash paid to suppliers and employees; partially offset by lower premium collections.

Increase in net purchases of investments in securities are part of our asset/liability management strategy using cash on hand.

Net capital expenditures increased by \$16.6 million for the year ended December 31, 2017 mostly related to information technology initiatives in the Managed Care segment.

During the year 2017, we received the remaining \$24.3 million from a loan with a commercial bank related with a credit agreement entered into in December 2016. These proceeds were used to prepay the outstanding principal amount of \$24.0 million of the 6.6% senior unsecured notes.

During the year 2017, the Company repurchased and retired 861,415 shares of our Class B Common Stock shares under the 2017 Repurchase Program. Repurchases were made at an average per share price of \$23.38, for an aggregate cost of \$20.2 million.

Stock Repurchase Program

The Company repurchases shares through open market transactions, in accordance with Rule 10b-18 of the Securities Exchange Act of 1934, as amended, under repurchase programs authorized by the Board of Directors. Shares purchased under share repurchase programs are retired and returned to authorized and unissued status. See Note 19, *Stock Repurchase Program*, of the Notes to Consolidated Financial Statements of this Annual Report.

Financing and Financing Capacity

We have several short-term facilities available to address timing differences between cash collections and disbursements. These short-term facilities are mostly in the form of arrangements to sell securities under repurchase agreements. As of December 31, 2018, we had \$60.0 million of available credit under these facilities. There are no outstanding short-term borrowings under these facilities as of December 31, 2018.

On December 28, 2016, TSM entered into a \$35.5 million credit agreement with a commercial bank in Puerto Rico. The agreement consists of three term loans: (i) Term Loan A in the principal amount of \$11.2 million, (ii) Term Loan B in the principal amount of \$20.2 million and (iii) Term Loan C in the principal amount of \$4.1 million. Term Loan A matures in October 2023 while the Term Loans B and C mature in January 2024. Term Loan A was used to refinance a previous \$41.0 million secured loan payable with the same commercial bank. Pursuant to the credit agreement, interest is payable on the outstanding balance of the Loan at the following annual rate: (i) 1% over LIBOR for Term Loan A, (ii) 2.75% over LIBOR for Term Loan B, and (iii) 3.25% over LIBOR for Term Loan C. The loan includes certain financial and non-financial covenants, which are customary for this type of facility, including but not limited to, restrictions on the granting of certain liens, limitations on acquisitions and limitations on changes in control and dividends. Failure to meet these covenants may trigger the accelerated payment of the outstanding balance. As of December 31, 2018 we are in compliance with these covenants.

On April 18, 2017, TSA entered into a \$10.0 million revolving loan agreement with a commercial bank in Puerto Rico. This line of credit has an interest rate of 30-day LIBOR plus 25 basis points contains certain financial and non-financial covenants that are customary for this type of facility. This line of credit had an original maturity date of April 17, 2018 and was renewed for an additional year, maturing on April 30, 2019.

We anticipate that we will have sufficient liquidity to support our currently expected needs.

Contractual Obligations

Our contractual obligations impact our short and long-term liquidity and capital resource needs. However, our future cash flow prospects cannot be reasonably assessed based solely on such obligations. Future cash outflows, whether contractual or not, will vary based on our future needs. While some cash outflows are completely fixed (such as commitments to repay principal and interest on borrowings), most are dependent on future events (such as the payout pattern of claim liabilities which have been incurred but not reported).

- The table below describes the payments due under our contractual obligations, aggregated by type of contractual obligation, including the maturity profile of our debt, operating leases and other long-term liabilities, but excludes an estimate of the future cash outflows related to the following:
 - Alternative investments – The Company has \$80.5 million of unfunded capital commitments related to alternative investments. These commitments were excluded from this disclosure due to the undetermined timing of their cash flows.
 - Unearned premiums – This amount accounts for the premiums collected prior to the end of coverage period and does not represent a future cash outflow. As of December 31, 2018, we had \$83.0 million in unearned premiums.

- Policyholder deposits – The cash outflows related to these instruments are not included because they do not have defined maturities, such that the timing of payments and withdrawals is uncertain. There are currently no significant policyholder deposits in paying status. As of December 31, 2018, our policyholder deposits had a carrying amount of \$174.1 million.
- Other long-term liabilities – Due to the indeterminate nature of their cash outflows, \$79.4 million of other long-term liabilities are not reflected in the following table, consisting of \$31.3 million of liability for pension benefits, \$3.2 million in deferred tax liabilities, and \$44.9 million in liabilities to the Federal Employees' Health Benefits Plan Program.

Contractual obligations by year

<i>(Dollar amounts in millions)</i>	Total	2019	2020	2021	2022	2023	Thereafter
Long-term borrowings (1)	\$ 33.0	\$ 4.1	\$ 4.2	\$ 4.0	\$ 3.9	\$ 3.5	\$ 13.3
Operating leases	11.3	5.2	3.0	1.7	1.2	0.2	-
Purchase obligations (2)	257.2	221.8	13.5	6.9	4.1	4.0	6.9
Claim liabilities (3)	611.8	483.7	95.0	7.8	9.5	6.3	9.5
Estimated obligation for future policy benefits (4)	670.6	131.2	117.6	111.7	105.7	100.2	104.2
	\$ 1,583.9	\$ 846.0	\$ 233.3	\$ 132.1	\$ 124.4	\$ 114.2	\$ 133.9

- (1) As of December 31, 2018, our long-term borrowings consist of a credit agreement entered with a commercial bank in Puerto Rico. See the "Financing and Financing Capacity" section for additional information regarding our long-term borrowings.
- (2) Purchase obligations represent payments required by us under material agreements to purchase goods or services that are enforceable and legally binding and where all significant terms are specified, including: quantities to be purchased, price provisions and the timing of the transaction. Other purchase orders made in the ordinary course of business for which we are not liable are excluded from the table above. Estimated pension plan contributions amounting to \$2.0 million were included within the total purchase obligations. However, this amount is an estimate which may be subject to change in view of the fact that contribution decisions are affected by various factors such as market performance, regulatory and legal requirements and plan funding policy.
- (3) Claim liabilities represent the amount of our claims processed and incomplete as well as an estimate of the amount of incurred but not reported claims and loss-adjustment expenses. This amount does not include an estimate of claims to be incurred subsequent to December 31, 2018. The expected claims payments are an estimate and may differ materially from the actual claims payments made by us in the future. Also, claim liabilities are presented gross, and thus do not reflect the effects of reinsurance under which \$325.0 million of reserves had been ceded at December 31, 2018.
- (4) Our Life segment establishes, and carries as liabilities, actuarially determined amounts that are calculated to meet its policy obligations when a policy matures or surrenders, an insured dies or becomes disabled or upon the occurrence of other covered events. A significant portion of the estimated obligation for future policy benefits to be paid included in this table considers contracts under which we are currently not making payments and will not make payments until the occurrence of an insurable event not under our control, such as death, illness, or the surrender of a policy. We have estimated the timing of the cash flows related to these contracts based on historical experience as well as expectations of future payment patterns. The amounts presented in the table above represent the estimated cash payments for benefits under such contracts based on assumptions related to the receipt of future premiums and assumptions related to mortality, morbidity, policy lapses, renewals, retirements, disability incidence and other contingent events as appropriate for the respective product type. All estimated cash payments included in this table are not discounted to present value nor do they take into account estimated future premiums on policies in-force as of December 31, 2018 and are gross of any reinsurance recoverable. The \$670.6 million total estimated cash flows for all years in the table is different from the liability of future policy benefits of \$361.5 million included in our audited consolidated financial statements principally due to the time value of money. Actual cash payments to policyholders could differ significantly from the estimated cash payments as presented in this table due to differences between actual experience and the assumptions used in the estimation of these payments.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, revenues and expenses, results of operations, liquidity, capital expenditures or capital resources.

Restriction on Certain Payments by the Corporation's Subsidiaries

Our insurance subsidiaries are subject to the regulations of the Commissioner of Insurance of Puerto Rico. These regulations, among other things, require insurance companies to maintain certain levels of capital, thereby restricting the amount of earnings that can be distributed by the insurance subsidiaries to TSM. As of December 31, 2018, our insurance subsidiaries, except for TSP, were in compliance with such minimum capital requirements. TSP is currently under a plan to increase its statutory capital and surplus and RBC scores.

These regulations are not directly applicable to TSM, as a holding company, since it is not an insurance company.

The \$35.5 million credit agreement limits the amount of dividends or other distributions (including share repurchases) payable by the Corporation to \$50 million per year.

We do not expect that any of the previously described dividend restrictions will have a significant effect on our ability to meet our cash obligations.

Solvency Regulation

To monitor the solvency of the operations, the BCBSA requires us, TSS, TSA, and TSB to comply with certain specified levels of Risk Based Capital ("RBC"). RBC is designed to identify weakly capitalized companies by comparing each company's adjusted surplus to its required surplus (RBC ratio). The RBC ratio reflects the risk profile of insurance companies. At December 31, 2018, TSM and TSS estimated RBC ratio was above the 375% minimum BCBSA RBC requirement to avoid monitoring. At December 31, 2018, TSA estimated RBC ratio was above the minimum BCBSA RBC requirement of 100% for smaller controlled affiliate.

BCBSA's primary licensees could be subject to monitoring if, over a 6 or 12 month period, its RBC ratio declines by 80 or more points and which results in a level that is below 500%.

Other Contingencies

Legal Proceedings

Various litigation claims and assessments against us have arisen in the course of our business, including but not limited to, our activities as an insurer and employer. Furthermore, the Commissioner of Insurance, as well as other Federal, Puerto Rico, and Costa Rica government authorities, regularly make inquiries and conduct audits concerning our compliance with applicable insurance and other laws and regulations.

Given the inherent unpredictability of these matters, it is possible that an adverse outcome in certain matters could, from time to time, have an adverse effect on our operating results and/or cash flows. For a description of our legal proceedings, see Note 24, *Contingencies*, of the Notes to Consolidated Financial Statements, included in this Annual Report.

Guarantee Associations and Other Regulatory Commitments

To operate in Puerto Rico, insurance companies, such as our insurance subsidiaries, are required to participate in guarantee associations, which are organized to pay policyholders contractual benefits on behalf of insurers declared insolvent. These associations levy assessments, up to prescribed limits, on a proportional basis, to all member insurers in the line of business in which the insolvent insurer was engaged. In accordance with insurance laws and regulations, assessments are recoverable through policy surcharges. In January 2019, a local property and casualty insurance company entered a liquidation

process, accordingly, the property and casualty guarantee fund has initiated the process to settle unpaid claims and return unearned premiums of the insolvent insurer. The guarantee fund currently has not determined and imposed assessments to cover claims and return premiums. Annual assessments are limited to 2% of direct premiums written, as defined. During 2018, 2017 and 2016, no assessment or payment was made for this contingency. It is the opinion of management that any possible future guarantee association assessments will not have a material effect on our operating results and/or cash flows, although there is no ceiling on these payment obligations.

Pursuant to the Puerto Rico Insurance Code, our Property and Casualty subsidiary is a member of Sindicato de Aseguradores para la Suscripción Conjunta de Seguros de Responsabilidad Profesional Médico-Hospitalaria (SIMED). The syndicate was organized for the purpose of underwriting medical-hospital professional liability insurance. As a member, the Property and Casualty segment shares risks with other member companies and, accordingly, is contingently liable in the event the syndicate cannot meet their obligations. During 2018, 2017 and 2016, no assessment or payment was made for this contingency. It is the opinion of management that any possible future syndicate assessments will not have a material effect on our operating results and/or cash flows, although there is no ceiling on these payment obligations. In December 2018, SIMED declared a distribution to its members; the Company's share of this distribution was \$2.9 million, which is presented with other income in the accompanying consolidated statement of earnings.

In addition, our Property and Casualty insurance subsidiary is a member of the Compulsory Vehicle Liability Insurance Joint Underwriting Association (the "Association"). The Association was organized in 1997 to underwrite insurance coverage of motor vehicle property damage liability risks effective January 1, 1998. As a participant, the segment shares the risk proportionally with other members based on a formula established by the Insurance Code. During the years 2018 and 2016, the Association distributed to the Company an amount based on the good experience of the business amounting to \$0.2 million and \$0.5 million, respectively. In June 2017, the Association declared a special dividend of \$70 million as authorized by a recent amendment to the Act creating the Association. The distribution was subject to a unique and special tax rate of 50%. The dividend was paid net of its related tax in December 2018. The share of the Property and Casualty segment in this distribution was \$2.4 million.

The Property and Casualty segment is also member of the Puerto Rico Fire and Allied Lines Underwriting Association and the Puerto Rico Auto Assign Plan. These entities periodically impose assessments to cover operations and other charges. The assessments recorded from these entities were \$9 thousand in 2018 and \$1 thousand in 2017 and 2016.

Critical Accounting Estimates

Our consolidated financial statements and accompanying notes included in this Annual Report on Form 10-K have been prepared in accordance with GAAP applied on a consistent basis. 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, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We continually evaluate the accounting policies and estimates we use to prepare our consolidated financial statements. In general, management's estimates are based on historical experience and various other assumptions it believes to be reasonable under the circumstances. The following is an explanation of our accounting policies considered most significant by management. These accounting policies require us to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Such estimates and assumptions could change in the future as more information is known. Actual results could differ materially from those estimates.

The policies discussed below are considered by management to be critical to an understanding of our consolidated financial statements because their application places the most significant demands on management's judgment, with financial reporting results relying on estimation about the effect of matters that are inherently uncertain. For all these policies, management cautions that future events may not necessarily develop as forecasted, and that the best estimates routinely require adjustment. Management believes that the amounts provided for these critical accounting estimates are adequate.

Claim Liabilities

Claim liabilities by segment as of December 31, 2018 were as follows:

(Dollar amounts in millions)

Managed care	\$	393.7
Property and casualty insurance		496.9
Life insurance		46.2
Consolidated	\$	936.8

Management continually evaluates the potential impact of changes in the factors considered for its claim liabilities estimates, both positive and negative, and uses the results of these evaluations to adjust recorded claim liabilities and underwriting criteria. Our profitability depends in large part on our ability to accurately predict and effectively manage the amount of claims incurred, particularly those of the Managed Care segment and the losses arising from the Life and Property and Casualty segments. Management regularly reviews its premiums and benefits structure to reflect our underlying claims experience and revised actuarial data; however, several factors could adversely affect our underwriting results. Some of these factors are beyond management's control and could adversely affect its ability to accurately predict and effectively control claims incurred. Examples of such factors include changes in health practices, economic conditions, change in utilization trends including those caused by epidemic conditions, healthcare costs, the advent of natural disasters, and malpractice litigation. Costs in excess of those anticipated could have a material adverse effect on our results of operations.

We recognize claim liabilities as follows:

Managed Care Segment

At December 31, 2018, claim liabilities for the Managed Care segment amounted to \$393.7 million and represented 42.0% of our total consolidated claim liabilities and 20.3% of our total consolidated liabilities.

Claim liabilities are determined employing actuarial methods that are commonly used by managed care actuaries and meet Actuarial Standards of Practice, which require that the claim liabilities be adequate under moderately adverse circumstances. The segment determines the amount of the liability by following a detailed actuarial process that entails using both historical claim payment patterns as well as emerging medical cost trends to project a best estimate of claim liabilities. Under this process, historical claims incurred dates are compared to actual dates of claims payment. This information is analyzed to create "completion" or "development" factors that represent the average percentage of total incurred claims that have been paid through a given date after being incurred. Completion factors are applied to claims paid through the financial statement date to estimate the ultimate claim expense incurred for the current period. Actuarial estimates of claim liabilities are then determined by subtracting the actual paid claims from the estimate of the total expected claims incurred. The majority of unpaid claims, both reported and unreported, for any period, are those claims which are incurred in the final months of the period. Since the percentage of claims paid during the period with respect to claims incurred in those months is generally very low, the above-described completion factor methodology is less reliable for such months. In order to complement the analysis to determine the unpaid claims, historical completion factors and payment patterns are applied to incurred and paid claims for the most recent twelve months and compared to the prior twelve month period. Incurred claims for the most recent twelve months also take into account recent claims expense levels and health care trend levels (trend factors). Using all of the above methodologies, our actuaries determine based on the different circumstances the unpaid claims as of the end of period.

Because the reserve methodology is based upon historical information, it must be adjusted for known or suspected operational and environmental changes. These adjustments are made by our actuaries based on their knowledge and their estimate of emerging impacts to benefit costs and payment speed.

Managed care claim liabilities also include a provision for adverse deviation, which is an estimate for known environmental factors that are reasonably likely to affect the required level of reserves. This provision for adverse deviation is intended to capture the potential adverse development from known environmental factors such as our entry into new geographical markets, changes in our geographic or product mix, the introduction of new customer populations, variation in benefit utilization, disease outbreaks, changes in provider reimbursement, fluctuations in medical cost trend, variation in claim submission patterns and variation in claims processing speed and payment patterns, changes in technology that provide faster access to claims data or change the speed of adjudication and settlement of claims, variability in claim inventory levels, non-standard claim development, and/or exceptional situations that require judgmental adjustments in setting the reserves for claims.

Circumstances to be considered in developing our best estimate of reserves include changes in enrollment, utilization levels, unit costs, mix of business, benefit plan designs, provider reimbursement levels, processing system conversions and changes, claim inventory levels, regulatory and legislative requirements, claim processing patterns, and claim submission patterns. A comparison of prior period liabilities to re-estimated claim liabilities based on subsequent claims development is also considered in making the liability determination. In the actuarial process, the methods and assumptions are not changed as reserves are recalculated, but rather the availability of additional paid claims information drives our changes in the re-estimate of the unpaid claim liability. Changes in such development are recorded as a change to current period benefit expense. The re-estimates or recasts are done monthly for the previous four calendar quarters. On average, about 91% of the claims are paid within three months after the last day of the month in which they were incurred and about 5% are within the next three months, for a total of 96% paid within six months after the last day of the month in which they were incurred.

Management regularly reviews its assumptions regarding claim liabilities and makes adjustments to claims incurred when necessary. If management's assumptions regarding cost trends and utilization are significantly different than actual results, our consolidated statement of earnings and financial position could be impacted in future periods. Changes to prior year estimates may result in an increase in claims incurred or a reduction of claims incurred in the period the change is made. Further, due to the considerable variability of health care costs, adjustments to claims liabilities are made in each period and are sometimes significant as compared to the net income recorded in that period. Prior year development of claim liabilities is recognized immediately upon the actuary's judgment that a portion of the prior year liability is no longer needed or that an additional liability should have been accrued. Health care trends are monitored in conjunction with the claim reserve analysis. Based on these analyses, rating trends are adjusted to anticipate future changes in health care cost or utilization. Thus, the Managed Care segment incorporates those trends as part of the development of premium rates in an effort to keep premium rating trends in line with claims trends.

As described above, completion factors and claims trend factors can have a significant impact on the determination of our claim liabilities. The following example provides the estimated impact on our December 31, 2018 claim liabilities, assuming the indicated hypothetical changes in completion and trend factors:

(Dollar amounts in millions)

Completion Factor ¹		Claims Trend Factor ²	
(Decrease) Increase		(Decrease) Increase	
In completion factor	In unpaid claim liabilities	In claims trend factor	In unpaid claim liabilities
-1.2%	\$20.3	1.5%	\$17.6
-0.8%	13.4	1.0%	11.7
-0.4%	6.7	0.5%	5.9
0.4%	(6.7)	-0.5%	(5.9)
0.8%	(13.3)	-1.0%	(11.7)
1.2%	(19.7)	-1.5%	(17.6)

(1) Assumes (decrease) increase in the completion factors for the most recent twelve months.

(2) Assumes (decrease) increase in the claims trend factors for the most recent twelve months.

The segments' reserving practice is to consistently recognize the actuarial best estimate as the ultimate liability for claims within a level of confidence required by actuarial standards. Management believes that the methodology for determining the best estimate for claim liabilities at each reporting date has been consistently applied.

Amounts incurred related to prior years vary from previously estimated liabilities as the claims are ultimately settled. Liabilities at any year-end are continually reviewed and re-estimated as information regarding actual claims payments, or run-out becomes known. This information is compared to the originally established year-end liability. Negative amounts reported for incurred claims related to prior years result from claims being settled for amounts less than originally estimated. The reverse is true of reserve shortfalls. Medical claim liabilities are usually described as having a "short tail", which means that they are generally paid within several months of the member receiving service from the provider. Accordingly, the majority, or approximately 93%, of any redundancy or shortfall relates to claims incurred in the previous calendar year-end, with the remaining 7% related to claims incurred prior to the previous calendar year-end. Management has not noted any significant emerging trends in claim frequency and severity and the normal fluctuations in enrollment and utilization trends from year to year.

The following table shows the variance between the segment's incurred claims for current period insured events and the incurred claims for such years had they been determined retrospectively (the "Incurred claims related to current period insured events" for the year shown plus or minus the "Incurred claims related to prior period insured events" for the following year as included in Note 11, *Claim Liabilities* and Claim Adjustment Expenses, of the Notes to Consolidated Financial Statements, included in Annual Report. This table shows that the segments' estimates of this liability have approximated the actual development.

<i>(Dollar amounts in millions)</i>	2017	2016	2015
Years ended December 31,			
Total incurred claims:			
As reported ⁽¹⁾	\$ 2,231.1	\$ 2,356.6	\$ 2,216.3
On a retrospective basis	2,195.1	2,343.8	2,207.3
Variance	\$ 36.0	\$ 12.8	\$ 9.0
Variance to total incurred claims as reported	1.6%	0.5%	0.4%

(1) Includes total claims incurred less adjustments for prior year reserve development.

Management expects that substantially all of the development of the 2018 estimate of medical claims payable will be known during 2019.

In the event this segment experiences an unexpected increase in health care cost or utilization trends, we have the following options to cover claim payments:

- Through the management of our cash flows and investment portfolio.
- In the Commercial business we have the ability to increase the premium rates throughout the year in the monthly renewal process, when renegotiating the premiums for the following contract year of each group as they become due. We consider the actual claims trend of each group when determining the premium rates for the following contract year.
- We have available short-term borrowing facilities that from time to time address differences between cash receipts and disbursements.

For additional information on our credit facilities, see section "*Financing and Financing Capacity*".

Life Segment

At December 31, 2018, claim liabilities for the life segment amounted to \$46.2 million and represented 5.0% of total consolidated claim liabilities and 2.4% of our total consolidated liabilities.

The claim liabilities related to the life segment are based on methods and underlying assumptions in accordance with GAAP. The estimate of claim liabilities for this segment is based on the amount of benefits contractually determined for reported claims, and on estimates based on past experience modified for current trends, for unreported claims. This estimate relies on observations of ultimate loss experience for similar historical events.

Claim reserve reviews are generally conducted on a monthly basis, in light of continually updated information. We review reserves using current inventory of policies and claims data. These reviews incorporate a variety of actuarial methods, judgments and analysis.

The key assumption with regard to claim liabilities for our life segment is related to claims incurred prior to the end of the year, but not yet reported to our subsidiary. A liability for these claims is estimated based upon experience with regards to amounts reported subsequent to the close of business in prior years. There are uncertainties in the development of these estimates; however, in recent years our estimates have resulted in immaterial redundancies or deficiencies.

Property and Casualty Segment

At December 31, 2018, claim liabilities for the Property and Casualty segment amounted to \$496.9 million and represented 53.0% of the total consolidated claim liabilities and 25.6% of our total consolidated liabilities. Claims liabilities related to losses caused by Hurricanes Irma and Maria amount to approximately \$415.9 million.

Estimates of the ultimate cost of claims and loss-adjustment expenses of this segment are based largely on the assumption that past developments, with appropriate adjustments due to known or unexpected changes, are a reasonable basis on which to predict future events and trends, and involve a variety of actuarial techniques that analyze current experience, trends and other relevant factors. Property and casualty insurance claim liabilities are categorized and tracked by line of business. Medical malpractice policies are written on a claims-made basis. Policies written on a claims-made basis require that claims be reported during the policy period. Other lines of business are written on an occurrence basis. Hurricane losses initially include the use of models from industry recognized firms having data, historical and current information about the events, to estimate ultimate losses. These estimates are supplemented by internal estimates of other costs deemed necessary to develop the ultimate losses. As loss information emerges, claims are separated between those with solid estimates and the remained claims. Additional reserves are provided based on paid loss experience for unreported, potential development, and loss expenses.

Individual case estimates for reported claims are established by a claims adjuster and are changed as new information becomes available during the course of handling the claim. Our property and casualty business, other than medical malpractice, is primarily short-tailed business, where losses (e.g. paid losses and case reserves) are generally reported quickly.

Claim reserve reviews are generally conducted on a quarterly basis, in light of continually updated information. Our actuary certifies reserves for both current and prior accident years using current claims data. These reviews incorporate a variety of actuarial methods, judgments, and analysis. For each line of business, a variety of actuarial methods are used, with the final selections of ultimate losses that are appropriate for each line of business selected based on the current circumstances affecting that line of business. These selections incorporate input from management, particularly from the claims, underwriting and operations divisions, about reported loss cost trends and other factors that could affect the reserve estimates.

Key assumptions are based on the consideration that past emergence of paid losses and case reserves is credible and likely indicative of future emergence and ultimate losses. A key assumption is the expected loss ratio for the current accident year. This expected loss ratio is generally determined through a review of the loss ratios of prior accident years and expected changes to earned pricing, loss costs, mix of business, and other factors that are expected to impact the loss ratio for the current accident year. Another key assumption is the development patterns for paid and reported losses (also referred to as the loss emergence and settlement patterns). The reserves for unreported claims for each year are determined after reviewing the indications produced by each actuarial projection method, which, in turn, rely on the expected paid and reported development patterns and the expected loss ratio for that year.

At December 31, 2018, the claim liabilities of the Property and Casualty segment fall within the actuarial reserve range determined by the actuaries. Management reviews the results of the reserve estimates in order to determine any appropriate adjustments in the recording of reserves. Adjustments to reserve estimates are made after management's consideration of numerous factors, including but not limited to the magnitude of the difference between the actuarial indication and the recorded reserves, improvement or deterioration of actuarial indications in the period, the maturity of the accident year, trends observed over the recent past and the level of volatility within a particular line of business. In general, changes are made more quickly to more mature accident years and less volatile lines of business. Varying the net expected loss ratio by +/-1% in all lines of business for the six most recent accident years would increase/decrease the claims incurred by approximately \$5.0 million.

Liability for Future Policy Benefits

Our Life segment establishes, and carries as liabilities, actuarially determined amounts that are calculated to meet its policy obligations when a policy matures or surrenders, an insured dies or becomes disabled or upon the occurrence of other covered events. We compute the amounts for actuarial liabilities in conformity with GAAP.

Liabilities for future policy benefits for whole life and term insurance products and active life reserves for accident and health products are computed by the net level premium method, using interest assumptions ranging from 3.90% to 5.75% and withdrawal, mortality, morbidity and maintenance expense assumptions appropriate at the time the policies were issued (or when a block of business was purchased, as applicable). Accident and health unpaid claim reserves are stated at amounts determined by estimates on individual claims and estimates of unreported claims based on past experience. Deferred annuity reserves are carried at the account value.

For deferred annuities, the liability for future policy benefits is equal to total policy account values. The liabilities for all other products are based upon a variety of actuarial assumptions that are uncertain. The most significant of these assumptions is the level of anticipated death and health claims. Other assumptions that are less significant to the appropriate level of the liability for future policy benefits are anticipated policy persistency rates, investment yields, and operating expense levels. These are reviewed frequently by our subsidiary's external actuaries, to assure that the current level of liabilities for future policy benefits is sufficient, in combination with anticipated future cash flows, to provide for all contractual obligations. For all products, except for deferred annuities, the basis for the liability for future policy benefits is established at the time of issuance of each contract and would only change if our experience deteriorates to the point that the level of the liability is not adequate to provide for future policy benefits. We do not currently expect that level of deterioration to occur.

Deferred Policy Acquisition Costs and Value of Business Acquired

Certain costs for acquiring life and property and casualty insurance business are deferred. Acquisition costs related to the Managed Care segment are expensed as incurred.

The costs of acquiring new life business, principally commissions, and certain variable underwriting and policy issue expenses of our Life segment, have been deferred. These costs, including value of business acquired ("VOBA") recorded upon our acquisitions of TSV and TSB, are amortized to income over the premium-paying period of the related whole life and term insurance policies in proportion to the ratio of the expected annual premium revenue to the expected total premium revenue, and over the anticipated lives of universal life policies in proportion to the ratio of the expected annual gross profits to the expected total gross profits. The expected premiums revenue and gross profits are based upon the same mortality and withdrawal assumptions used in determining the liability for future policy benefits. For universal life and deferred annuity policies, changes in the amount or timing of expected gross profits result in adjustments to the cumulative amortization of these costs. The effect on the amortization of deferred policy acquisition costs ("DPAC" or "DAC") of revisions to estimated gross profits is reported in earnings in the period such estimated gross profits are revised.

The schedules of amortization of life insurance DPAC and VOBA are based upon actuarial assumptions regarding future events that are uncertain. For all products, other than universal life and deferred annuities, the most significant of these assumptions is the level of contract persistency and investment yield rates. For these products the basis for the amortization of DPAC and VOBA is established at the issue of each contract and would only change if our segment's experience deteriorates to the point that the level of the net liability is not adequate. We do not currently expect that level of deterioration to occur. For the universal life and deferred annuity products, amortization schedules are based upon the level of historic and anticipated gross profit margins, from the date of each contract's issued (or purchase, in the case of VOBA). These schedules are based upon several actuarial assumptions that are uncertain, are reviewed annually and are modified if necessary. The most significant of these assumptions are claims, investment yield rates and contract persistency. Based upon the most recent actuarial reviews of all of the assumptions, we do not currently anticipate material changes to the level of these amortization schedules.

The property and casualty business acquisition costs consist of commissions net of reinsurance commissions, during the production of business are deferred and amortized ratably over the terms of the policies. The method used in calculating deferred acquisition costs limits the amount of such deferred costs to actual costs or their estimated realizable value, whichever is lower.

Impairment of Investments

Impairment of an investment exists if a decline in the estimated fair value is below the amortized cost of the security. Management regularly monitors and evaluates the difference between the cost and estimated fair value of fixed maturity investments and other invested assets. For investments with a fair value below cost, the process includes evaluating: (1) the length of time and the extent to which the estimated fair value has been less than amortized cost for fixed maturity securities, or cost for equity securities, (2) the financial condition, near-term and long-term prospects for the issuer, including relevant industry conditions and trends, and implications of rating agency actions, (3) the Company's intent to sell or the likelihood of a required sale prior to recovery, (4) the recoverability of principal and interest for fixed maturity securities, or cost for equity securities, and (5) other factors, as applicable. This process is not exact and further requires consideration of risks such as credit and interest rate risks. Consequently, if an investment's cost exceeds its estimated fair value solely due to changes in interest rates, other-than temporary impairment may not be appropriate.

Due to the subjective nature of our analysis, along with the judgment that must be applied in the analysis, it is possible that we could reach a different conclusion whether or not to impair a security if we had access to additional information about the investee. Additionally, it is possible that the investee's ability to meet future contractual obligations may be different than what we determined during its analysis, which may lead to a different impairment conclusion in future periods.

If after monitoring and analyzing impaired securities, management determines that a decline in the estimated fair value of any fixed maturity security or other invested asset below cost is other than temporary, the carrying amount of the security is reduced to its fair value according to current accounting guidance. The new cost basis of an impaired security is not adjusted for subsequent increases in estimated fair value. In periods subsequent to the recognition of an other-than-temporary impairment, the impaired security is accounted for as if it had been purchased on the measurement date of the impairment. For debt securities, the discount (or reduced premium) based on the new cost basis may be accreted into net investment income in future periods based on prospective changes in cash flow estimates, to reflect adjustments to the effective yield.

Management reviews investment portfolios under our impairment review policy. Given current market conditions and the significant judgments involved, there is a continuing risk that further declines in fair value may occur and material other-than-temporary impairments may be recorded in future periods. Management from time to time may sell investments as part of its asset/liability management process or to reposition its investment portfolio based on current and expected market conditions.

During the year ended December 31, 2018, we were not required to recognize an other-than-temporary impairment. During the years ended December 31, 2017 and 2016, we recognized other-than-temporary impairments on equity securities amounting to \$49 thousand and \$1.4 million, respectively. The impairment analysis indicated that, none of the securities whose carrying amount exceeded its estimated fair value was considered other-than-temporarily impaired as of that date; however, several factors are beyond management's control, such as the following: financial condition of the issuers, movement of interest rates, specific situations within corporations, among others. Over time, the economic and market environment may provide additional insight regarding the estimated fair value of certain securities, which could change management's judgment regarding impairment. This could result in realized losses related to other-than-temporary declines being charged against future income.

Our fixed maturity securities are sensitive to interest rate and credit risk fluctuations, which impact the fair value of individual securities. Our equity securities are sensitive to equity price risks, for which potential losses could arise from adverse changes in the value of equity securities. For additional information on the sensitivity of our investments, see "*Quantitative and Qualitative Disclosures About Market Risk*" in this Annual Report.

A detail of the gross unrealized losses on investment securities and the estimated fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2018 and 2017 is included in Note 3, *Investment in Securities*, of the Notes to Consolidated Financial Statements, included in this Annual Report.

Allowance for Doubtful Receivables

We estimate the amount of uncollectible receivables in each period and establish an allowance for doubtful receivables considering, among other things, the continued deterioration of the local economy, the exposure to government accounts and the challenging business environment in the Island. The allowance for doubtful receivables amounted to \$42.0 million and \$35.9 million as of December 31, 2018 and 2017, respectively. As of December 31, 2018 and 2017, the Company had premiums and other receivables of \$54.3 million and \$81.8 million, respectively, from the Government of Puerto Rico, including its agencies, municipalities, and public corporations. The related allowance for doubtful receivables as of December 31, 2018 and 2017 was \$21.0 million and \$16.4 million, respectively. The amount of the allowance is based on the aging of unpaid accounts, information about the customer's creditworthiness and other relevant information. The estimates of uncollectible accounts are revised each period, and changes are recorded in the period they become known. In determining the allowance, we use predetermined percentages applied to aged account balances, as well as individual analysis of large accounts. These percentages are based on our collection experience and are periodically evaluated. A significant change in the level of uncollectible accounts would have a material effect on our results of operations.

In addition to premium-related receivables, we evaluate the risk in the realization of other accounts receivable, including balances due from third parties related to overpayment of medical claims and rebates, among others. These amounts are individually analyzed, and the allowance determined based on the specific collectivity assessment and circumstances of each individual case.

We consider this allowance adequate to cover probable losses that may result from our inability to subsequently collect the amounts reported as accounts receivable. However, such estimates may change significantly in the event that unforeseen economic conditions adversely impact the ability of third parties to repay the amounts due to us.

Goodwill and Other Intangible Assets

Our consolidated goodwill and other intangible assets at December 31, 2018 were \$25.4 million and \$2.6 million, respectively. At December 31, 2017 the consolidated goodwill and other intangible assets were \$25.4 million and \$3.6 million, respectively. The goodwill and other intangible assets balance for both years were primarily related to the acquisition of TSA in 2011. As of December 31, 2018 and 2017, the goodwill related to TSA was \$25.0 million. As of December 31, 2018 and 2017 other intangible assets related to the TSA acquisition were \$2.6 million and \$3.5 million, respectively.

We account for goodwill and intangible assets with indefinite lives in accordance with Accounting Standard Codification (ASC) No. 350, Goodwill and Other Intangible Assets, which specifies the types of acquired intangible assets that are required to be recognized and reported separately from goodwill. Under this guidance, goodwill is not amortized but is tested for impairment at least annually and more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. For goodwill, the impairment determination is made at the reporting unit level and consists of two steps.

Our impairment tests involve the use of estimates related to the fair value of the reporting unit and require a significant degree of management judgment and the use of subjective assumptions. The Company assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. If determined to be necessary, the two-step impairment test is used to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any). First, the Company determines the fair value of a reporting unit and compares it to its carrying amount. Second, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating

the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill.

Our goodwill impairment test uses the income approach to estimate a reporting unit's fair value. Use of the income approach for our goodwill impairment test reflects our view that valuation methodology provides a reasonable estimate of fair value. The income approach is developed using assumptions about future premiums, expected claims, MLR, operating expenses and net income derived from our internal planning process and historical trends. The Company also uses the market approach as part of their impairment analysis. These estimated future cash flows are then discounted. Our assumed discount rate is based on our industry's weighted average cost of capital. It assumes the effective implementation of measures to contain the utilization and cost trends. Events or changes in circumstances, including a decrease in membership, an increase in MLR and/or operating expenses, could result in goodwill impairment.

We completed our annual impairment tests of existing goodwill during the fourth quarter of 2018 and 2017. Limited interim impairment tests are also performed when potential impairment indicators exist or other changes in our business occur. If we do not achieve our earnings objectives or the cost of capital rises significantly, the assumptions and estimates underlying these impairment evaluations could be adversely affected and result in future impairment charges that would negatively impact our operating results. On the other hand, since October 2016 the TSA HMO contract scored 4.0 overall on a 5.0 star rating system, increasing 1.0 versus the prior year, and achieved 5 stars in Part D, which generated additional premiums in 2018. Furthermore, in October 2018, the TSA HMO product increased its overall score to 4.5 stars and the PPO contract increased its overall score to 4.0 stars, which are expected to further increase Medicare premiums for 2020. The result of the impairment test performed in 2018 and 2017 indicated that the fair value of the TSA unit exceeded its carrying value by approximately 62% and 26%, respectively.

While we believe we have appropriately allocated the purchase price of our acquisitions, this allocation requires many assumptions to be made regarding the fair value of assets and liabilities acquired. In addition, estimated fair values developed based on our assumptions and judgments might be significantly different if other reasonable assumptions and estimates were to be used. If estimated fair values are less than the carrying values of the reporting unit or if significant impairment indicators are noted relative to other intangible assets subject to amortization, we may be required to record impairment losses against future income.

Other Significant Accounting Policies

We have other accounting policies that are important to an understanding of the consolidated financial statements. See Note 2, *Significant Accounting Policies*, of the Notes to Consolidated Financial Statements, included in this Annual Report.

Recently Issued Accounting Standards

For a description of our recently issued accounting standards, see Note 2, *Significant Accounting Policies*, of the Notes to Consolidated Financial Statements, included in this Annual Report.

Quantitative and Qualitative Disclosures About Market Risk

We are exposed to certain market risks that are inherent in our financial instruments, which arise from transactions in the normal course of business. We are also subject to additional market risk with respect to certain of our financial instruments. We must effectively manage, measure, and monitor the market risk associated with our invested assets and interest rate sensitive liabilities. We have established and implemented comprehensive policies and procedures to minimize the effects of potential market volatility.

Market Risk Exposure

We have exposure to market risk mostly in our investment activities. For purposes of this disclosure, “market risk” is defined as the risk of loss resulting from changes in interest rates and equity prices. Analytical tools and monitoring systems are in place to assess each one of the elements of market risks.

Our investment portfolio consists mainly of investment grade fixed income and a smaller portion is held in equity securities and alternative investments. The investment portfolio is conservative, diversified across and within asset classes, and has the following objectives, in order of importance: capital preservation, liquidity, income generation and capital appreciation. The interest rate risk of both our investments and liabilities is regularly evaluated.

The investment portfolio is centrally managed by investment professionals and decisions are taken based on the guidelines and limitations described in our Investment Policy and the Puerto Rico Insurance Code. The Investment Policy is approved by the Board of Directors following the recommendation of the Investment and Financing Committee of the Board of Directors (the “Investment and Financing Committee”). The Investment and Financing Committee establishes guidelines to ensure the Investment Policy is adhered to and any exception must be reported to the Investment and Financing Committee.

We use a sensitivity analysis to measure the market risk related to our holdings of invested assets and other financial instruments. This analysis estimates the potential changes in fair value of the instruments subject to market risk. This sensitivity analysis is an estimate and should not be viewed as predictive of our future financial performance. Our actual losses in any year could exceed the amounts indicated in the following paragraphs. Limitations related to this sensitivity analysis include:

- the market risk information is limited by the assumptions and parameters established in creating the related sensitivity analysis, including the impact of prepayment rates on mortgages; and
- the model assumes that the composition of assets and liabilities remains unchanged throughout the year.

Accordingly, we use such models as tools and not as a substitute for the experience and judgment of our management.

Interest Rate Risk

Our exposure to interest rate changes results from our significant holdings of fixed maturity securities. We are also exposed to interest rate risk from our variable interest secured term loan and from our policyholder deposits.

Equity Price Risk

Our investments in equity securities expose us to price risks, for which potential losses could arise from adverse changes in the value of these investments.

Risk Measurement

Our investment securities are a source of market risk. As of December 31, 2018 approximately 77% of our investment portfolio consisted of fixed maturity securities. The remaining balance is comprised of equity securities and alternative investments. Our fixed maturity securities classified as available-for-sale and alternative investments are recorded at fair value and changes in the fair value of these securities, net of the related tax effect, are excluded from operations and are reported as a separate component of other comprehensive income (loss) until realized. Fixed maturity securities classified as held-to-maturity are recorded at amortized cost and adjusted for the amortization or accretion of premiums or discounts. Equity securities are recorded at fair value and changes in fair value are included in earnings. The fair value of the investments in our available-for-sale and held-to-maturity portfolios is exposed to both interest rate risk and equity price risk.

Interest Rate Risk

We have evaluated the net impact to the fair value of our fixed income investments of a significant one-time change in interest rate risk using a combination of both statistical and fundamental methodologies. From these shocked values, a resultant market price appreciation/depreciation can be determined after portfolio cash flows are modeled and evaluated over instantaneous 100, 200, and 300 basis point rate shifts. Techniques used in the evaluation of cash flows include Monte Carlo simulation through a series of probability distributions over 200 interest rate paths. Necessary prepayment speeds are compiled using Yield Book, which sources numerous factors in deriving speeds, including but not limited to: historical speeds, economic indicators, street consensus speeds, etc. Securities evaluated by us under these scenarios include mortgage pass-through certificates and collateralized mortgage obligations of U.S. agencies, and private label structures, if cash flows information is available. The following table sets forth the result of this analysis for the years ended December 31, 2018 and 2017. The analysis does not consider any action that management can take to mitigate the impact of changes in market rates.

(Dollar amounts in millions)

Change in Interest Rates	Expected Fair Value	Amount of Decrease	% Change
December 31, 2018:			
Base Scenario	\$ 1,202.0		
+100 bp	1,148.2	(53.8)	(4.5)%
+200 bp	1,097.9	(104.1)	(8.7)%
+300 bp	1,049.4	(152.6)	(12.7)%
December 31, 2017:			
Base Scenario	\$ 1,219.3		
+100 bp	1,163.4	(55.9)	(4.6)%
+200 bp	1,111.7	(107.6)	(8.9)%
+300 bp	1,062.4	(156.9)	(13.0)%

We believe that an interest rate shift in a 12-month period of 100 basis points represents a moderately adverse outcome, while a 200 basis point shift is significantly adverse and a 300 basis point shift is less likely given historical precedents. Although we classify 99.8% of our fixed maturity securities as available-for-sale, our cash flows and the intermediate duration of our investment portfolio should allow us to hold securities until maturity, thereby avoiding the recognition of losses, should interest rates rise significantly.

Equity Price Risk

Our equity securities are composed of mutual funds whose underlying assets are comprised of domestic equity securities, domestic preferred equity securities, international equity securities and higher risk fixed income instruments. The fixed income mutual funds invest mainly in loan participations and high yield debt. The securities in these funds are issued by corporations, financial institutions and governmental

entities that are either unrated or have non-investment grade ratings from either Standard & Poor's or Moody's.

Our investments in mutual funds exposes us to equity price risk and credit risk. We manage these exposures by closely monitoring the performance of these mutual funds.

Assuming an immediate decrease of 10% in the market value of our equity securities as of December 31, 2018 and 2017, the hypothetical loss in the fair value of these investments would have been approximately \$27.9 million and \$34.2 million, respectively.

Alternative Price Risk

Our alternative investments in the available-for-sale portfolio are comprised of commitments to limited liability partnerships. These private funds call capital over time and invest in various asset classes such as traditional private equity, infrastructure equity, real estate debt and corporate debt. These investments are unrated, illiquid and expose us to a variety of underlying risks. We manage these exposures by closely monitoring the performance of these funds. The fair value of alternative investments is estimated using the net asset value of the Company's ownership interest in the partnerships as a practical expedient to determining an independent fair value.

Assuming an immediate decrease of 10% in the market value of our equity securities as of December 31, 2018 and 2017, the hypothetical loss in the fair value of these investments would have been approximately \$7.4 million and \$3.5 million, respectively.

Other Risk Measurement

We are subject to interest rate risk on our variable interest secured term loan and our policyholder deposits. Shifting interest rates do not have a material effect on the fair value of these instruments. The secured term loan has a variable interest rate structure, which reduces the potential exposure to interest rate risk. The policyholder deposits have short-term interest rate guarantees, which also reduce the accounts' exposure to interest rate risk.

Triple-S Management Corporation and Subsidiaries

**Consolidated Financial Statements
December 31, 2018, 2017, and 2016**

To Our Stockholders

Management's Report on Internal Control Over Financial Reporting

The management of Triple-S Management Corporation (the Company) is responsible for establishing and maintaining adequate internal control over financial reporting and for the assessment of the effectiveness of "internal control over financial reporting," as defined under Exchange Act Rule 13a-15(f). The Company's internal control over financial reporting is a process designed by, or under the supervision of, the Company's Chief Executive Officer and Chief Financial Officer, and effected by the Company's Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's consolidated financial statements for external purposes in accordance with Generally Accepted Accounting Principles (GAAP), and includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the consolidated financial statements.

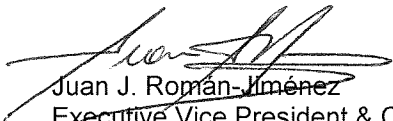
Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management, under the supervision and with the participation of the Chief Financial Officer and Chief Executive Officer, assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2018, based on criteria described in the "Internal Control—Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) on May 14, 2013. Based on that assessment and those criteria, management has concluded that the Company's internal control over financial reporting was effective as of December 31, 2018 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's consolidated financial statements for external reporting purposes in accordance with GAAP.

The effectiveness of our internal control over financial reporting as of December 31, 2018 has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report, which appears herein.



Roberto García-Rodríguez
President & CEO



Juan J. Román-Jiménez
Executive Vice President & CFO

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of Triple-S Management Corporation

Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of Triple-S Management Corporation and its subsidiaries (the "Company") as of December 31, 2018, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements as of and for the year ended December 31, 2018, of the Company and our report dated February 28, 2019, expressed an unqualified opinion on those financial statements.

Basis for Opinion


The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The logo for Deloitte & Touche LLP, featuring the company name in a stylized, cursive script.

February 28, 2019
Stamp No. E360679
affixed to original.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of Triple-S Management Corporation

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Triple-S Management Corporation and its subsidiaries (the "Company") as of December 31, 2018 and 2017, the related consolidated statements of earnings, comprehensive income, stockholders' equity, and cash flows, for each of the three years in the period ended December 31, 2018, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 28, 2019, expressed an unqualified opinion on the Company's internal control over financial reporting.

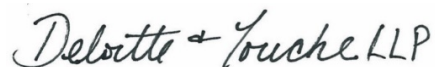
Change in Accounting Principle

As discussed in Note 2 to the financial statements, the Company has changed its method of accounting for unrealized holding gains and losses on equity investments in 2018 due to the adoption of Financial Accounting Standards Board Accounting Standards Update 2016-01, *Recognition and measurement of financial assets and financial liabilities*.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

The logo for Deloitte & Touche LLP, featuring the company name in a stylized, cursive script.

February 28, 2019
Stamp No. E360678
affixed to original.

We have served as the Company's auditor since 2015.

Triple-S Management Corporation and Subsidiaries
Consolidated Balance Sheets
December 31, 2018 and 2017

(dollar amounts in thousands, except share data)

Assets	2018	2017
Investments and cash		
Fixed maturities available for sale, at fair value (amortized cost of \$1,168,369 in 2018 and \$1,171,651 in 2017)	\$ 1,199,402	\$ 1,216,788
Fixed maturities held to maturity, at amortized cost (fair value of \$2,619 in 2018 and \$2,475 in 2017)	2,492	2,319
Equity investments, at fair value (cost of \$265,858 in 2018 and \$292,459 in 2017)	279,164	342,308
Other invested assets, at net asset value (amortized cost of \$72,627 in 2018 and \$34,670 in 2017)	74,015	34,985
Policy loans	9,469	9,077
Cash and cash equivalents	117,544	198,941
Total investments and cash	<u>1,682,086</u>	<u>1,804,418</u>
Premium and other receivables, net	628,444	899,327
Deferred policy acquisition costs and value of business acquired	215,159	200,788
Property and equipment, net	81,923	74,716
Deferred tax asset	79,010	65,123
Goodwill	25,397	25,397
Other assets	48,229	46,996
Total assets	<u>\$ 2,760,248</u>	<u>\$ 3,116,765</u>
Liabilities and Stockholders' Equity		
Claim liabilities	\$ 936,789	1,106,876
Liability for future policy benefits	361,495	339,507
Unearned premiums	82,990	86,349
Policyholder deposits	174,110	176,534
Liability to Federal Employees' Health Benefits and Federal Employees' Programs	44,926	52,287
Accounts payable and accrued liabilities	275,228	354,894
Deferred tax liability	3,245	21,891
Long term borrowings	28,883	32,073
Liability for pension benefits	31,274	33,672
Total liabilities	<u>1,938,940</u>	<u>2,204,083</u>
Commitments and contingencies		
Stockholders' equity		
Triple-S Management Corporation stockholders' equity		
Common stock Class A, \$1 par value. Authorized 100,000,000 shares; issued and outstanding 950,968 at December 31, 2018 and 2017	951	951
Common stock Class B, \$1 par value. Authorized 100,000,000 shares; issued and outstanding 21,980,492 and 22,627,077 shares at December 31, 2018 and 2017, respectively	21,980	22,627
Additional paid-in capital	34,021	53,142
Retained earnings	761,970	785,390
Accumulated other comprehensive income, net	3,062	51,254
Total Triple-S Management Corporation stockholders' equity	<u>821,984</u>	<u>913,364</u>
Non-controlling interest in consolidated subsidiary	(676)	(682)
Total stockholders' equity	<u>821,308</u>	<u>912,682</u>
Total liabilities and stockholders' equity	<u>\$ 2,760,248</u>	<u>\$ 3,116,765</u>

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

Triple-S Management Corporation and Subsidiaries
Consolidated Statements of Earnings
December 31, 2018, 2017, and 2016

(dollar amounts in thousands, except per share data)

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Revenues:			
Premiums earned, net	\$ 2,938,591	\$ 2,826,932	\$ 2,890,641
Administrative service fees	14,701	16,514	17,843
Net investment income	61,909	51,615	48,913
Other operating revenues	5,794	3,660	3,461
Total operating revenues	<u>3,020,995</u>	<u>2,898,721</u>	<u>2,960,858</u>
Net realized investment gains (losses):			
Total other-than-temporary impairment losses on securities	-	(49)	(1,434)
Net realized gains, excluding other-than-temporary impairment losses on securities	298	10,880	18,813
Total net realized investment gains	<u>298</u>	<u>10,831</u>	<u>17,379</u>
Net unrealized investment losses on equity investments	(36,546)	-	-
Other income, net	11,312	6,533	6,569
Total revenues	<u>2,996,059</u>	<u>2,916,085</u>	<u>2,984,806</u>
Benefits and expenses:			
Claims incurred, net of reinsurance	2,527,613	2,353,101	2,472,191
Operating expenses	554,715	477,213	493,894
Total operating costs	<u>3,082,328</u>	<u>2,830,314</u>	<u>2,966,085</u>
Interest expense	6,903	6,794	7,635
Total benefits and expenses	<u>3,089,231</u>	<u>2,837,108</u>	<u>2,973,720</u>
(Loss) income before taxes	<u>(93,172)</u>	<u>78,977</u>	<u>11,086</u>
Income tax (benefit) expense	(29,866)	24,496	(6,345)
Net (loss) income	<u>(63,306)</u>	<u>54,481</u>	<u>17,431</u>
Less: Net loss attributable to non-controlling interest	4	5	7
Net (loss) income attributable to Triple-S Management Corporation	<u>\$ (63,302)</u>	<u>\$ 54,486</u>	<u>\$ 17,438</u>
Earnings per share attributable to Triple-S Management Corporation			
Basic net (loss) income per share	\$ (2.76)	\$ 2.27	\$ 0.71
Diluted net (loss) income per share	\$ (2.76)	\$ 2.26	\$ 0.71

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

Triple-S Management Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income
December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Net (loss) income	\$ (63,306)	\$ 54,481	\$ 17,431
Other comprehensive (loss) income, net of tax:			
Net unrealized change in fair value of available for sale securities, net of taxes	(9,048)	13,867	(107)
Defined benefit pension plan:			
Actuarial gain (loss), net	738	(5,028)	18,232
Prior service credit, net	-	20	(1,353)
Total other comprehensive income, net of tax	<u>(8,310)</u>	<u>8,859</u>	<u>16,772</u>
Comprehensive (loss) income	<u>(71,616)</u>	<u>63,340</u>	<u>34,203</u>
Comprehensive loss attributable to non-controlling interest	4	5	7
Comprehensive (loss) income attributable to Triple-S Management Corporation	\$ (71,612)	\$ 63,345	\$ 34,210

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

Triple-S Management Corporation and Subsidiaries

Consolidated Statements of Stockholders' Equity

December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

	Class A Common Stock	Class B Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Triple-S Management Corporation Stockholders' Equity	Non-controlling Interest in Consolidated Subsidiary	Total Stockholders' Equity
Balance, December 31, 2015	\$ 951	\$ 24,048	\$ 83,438	\$ 713,466	\$ 25,623	\$ 847,526	\$ (670)	\$ 846,856
Share-based compensation	-	223	2,576	-	-	2,799	-	2,799
Stock issued upon exercise of stock options	-	4	51	-	-	55	-	55
Repurchase and retirement of common stock	-	(954)	(20,473)	-	-	(21,427)	-	(21,427)
Comprehensive income (loss)	-	-	-	17,438	16,772	34,210	(7)	34,203
Balance, December 31, 2016	\$ 951	\$ 23,321	\$ 65,592	\$ 730,904	\$ 42,395	\$ 863,163	\$ (677)	\$ 862,486
Share-based compensation	-	167	6,909	-	-	7,076	-	7,076
Repurchase and retirement of common stock	-	(861)	(19,359)	-	-	(20,220)	-	(20,220)
Comprehensive income (loss)	-	-	-	54,486	8,859	63,345	(5)	63,340
Balance, December 31, 2017	\$ 951	\$ 22,627	\$ 53,142	\$ 785,390	\$ 51,254	\$ 913,364	\$ (682)	\$ 912,682
Share-based compensation	-	287	3,070	-	-	3,357	-	3,357
Repurchase and retirement of common stock	-	(934)	(22,191)	-	-	(23,125)	-	(23,125)
Comprehensive income (loss)	-	-	-	(63,302)	(8,310)	(71,612)	6	(71,606)
Cumulative effect adjustment due to implementation of ASU 2016-01	-	-	-	39,882	(39,882)	-	-	-
Balance, December 31, 2018	\$ 951	\$ 21,980	\$ 34,021	\$ 761,970	\$ 3,062	\$ 821,984	\$ (676)	\$ 821,308

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

Triple-S Management Corporation and Subsidiaries
Consolidated Statements of Cash Flows
December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Cash flows from operating activities			
Net (loss) income	\$ (63,306)	\$ 54,481	\$ 17,431
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	13,535	13,198	14,120
Net amortization of investments	3,976	10,114	8,671
Additions to the allowance for doubtful receivables	11,321	1,462	1,601
Deferred tax benefit	(32,078)	(9,916)	(8,326)
Net realized investment gains on sale of securities	(298)	(10,831)	(17,379)
Net unrealized loss on equity investments	36,546	-	-
Interest credited to policyholder deposits	5,722	5,677	3,794
Share-based compensation	3,357	7,076	2,463
(Increase) decrease in assets			
Premium and other receivables, net	259,561	(614,424)	(5,320)
Deferred policy acquisition costs and value of business acquired	(12,258)	(6,596)	(7,286)
Deferred taxes	946	4,946	(4,799)
Other assets	(1,470)	5,117	(9,009)
Increase (decrease) in liabilities			
Claim liabilities	(170,087)	618,933	(3,822)
Liability for future policy benefits	21,988	18,275	31,702
Unearned premiums	(3,359)	7,039	(950)
Liability to FEHBP	(7,361)	17,917	7,675
Accounts payable and accrued liabilities	(59,276)	166,450	(24,095)
Net cash provided by operating activities	<u>7,459</u>	<u>288,918</u>	<u>6,471</u>

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

Triple-S Management Corporation and Subsidiaries
Consolidated Statements of Cash Flows
December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Cash flows from investing activities			
Proceeds from investments sold or matured			
Securities available for sale:			
Fixed maturities sold	\$ 1,302,810	\$ 463,232	\$ 400,848
Fixed maturities matured	24,945	18,893	56,988
Securities held to maturity:			
Fixed maturities matured	8,182	2,712	1,538
Equity investments sold	203,841	59,963	109,049
Other invested assets sold	3,714	-	-
Acquisition of investments			
Securities available for sale			
Fixed maturities	(1,343,346)	(560,304)	(482,252)
Securities held to maturity			
Fixed maturities	(8,356)	(2,197)	(1,445)
Equity investments	(156,486)	(134,834)	(163,119)
Other invested assets	(47,221)	-	-
Other investments	(705)	(2,064)	(2,493)
Net disbursements for policy loans	(392)	(513)	(663)
Net capital expenditures	(19,840)	(21,359)	(4,750)
Net cash used in investing activities	<u>(32,854)</u>	<u>(176,471)</u>	<u>(86,299)</u>
Cash flows from financing activities			
Change in outstanding checks in excess of bank balances	(22,243)	12,683	12,250
Repayments of long-term borrowings	(3,236)	(2,836)	(1,742)
Repurchase and retirement of common stock	(22,377)	(20,220)	(21,371)
Net proceeds from revolving line of credit	-	1,964	-
Proceeds from policyholder deposits	18,531	13,557	18,224
Surrenders of policyholder deposits	(26,677)	(22,082)	(21,923)
Net cash used in financing activities	<u>(56,002)</u>	<u>(16,934)</u>	<u>(14,562)</u>
Net (decrease) increase in cash and cash equivalents	<u>(81,397)</u>	<u>95,513</u>	<u>(94,390)</u>
Cash and cash equivalents			
Beginning of year	198,941	103,428	197,818
End of year	<u>\$ 117,544</u>	<u>\$ 198,941</u>	<u>\$ 103,428</u>

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

Triple-S Management Corporation and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

1. Nature of Business

Triple-S Management Corporation (the Corporation, the Company or TSM) was incorporated under the laws of the Commonwealth of Puerto Rico to engage, among other things, as the holding company of entities primarily involved in the insurance industry.

The Company has the following wholly owned subsidiaries: (1) Triple-S Salud, Inc. (TSS) and Triple-S Advantage, Inc. (TSA), are managed care organizations that provide health benefits services to subscribers through contracts with hospitals, physicians, dentists, laboratories, and other organizations; (2) Triple-S Vida, Inc. (TSV) and Triple-S Blue, Inc. (TSB), are engaged in the underwriting of life and accident and health insurance policies and the administration of annuity contracts; and (3) Triple-S Propiedad, Inc. (TSP), is engaged in the underwriting of property and casualty insurance policies. The Company, TSS and TSA are members of the Blue Cross and Blue Shield Association (BCBSA). The Company and the above mentioned subsidiaries are subject directly or indirectly to the regulations of the Commissioner of Insurance of the Commonwealth of Puerto Rico (the Commissioner of Insurance), the General Superintendence of Insurance of Costa Rica, the U.S. Virgin Islands (USVI), the British Virgin Islands (BVI) Financial Services Commission, and the Anguilla Financial Services Commission.

The Company also owns a controlling interest in a health clinic in Puerto Rico, as part of our strategic initiatives. Besides its current operations, this health clinic owns controlling interests in other health clinics throughout the island.

Through our subsidiary TSS, we provide services to participants of the Commonwealth of Puerto Rico Health Insurance Plan (similar to Medicaid) (Medicaid). On September 21, 2018, TSS entered into a contract with the Puerto Rico Health Insurance Administration (ASES by its Spanish acronym), as one of the five managed care organizations (MCOs), that offer health care services to Medicaid and Child Health Insurance subscribers for the government of Puerto Rico's revised Medicaid health insurance program. The contract is effective from November 1, 2018 up to September 30, 2021, which term may be extended an additional year at ASES's option. The revised delivery model requires MCOs to serve subscribers in an island-wide basis, rather than through the assignment of specific regions within the Island. Under the new agreement, TSS is responsible for the provision of medical, mental, pharmacy, and dental healthcare services on an at-risk basis to subscribers who enroll with TSS. ASES will pay TSS a per member per month rate that will vary depending on the clinical condition or category of the subscriber and initially assigned TSS approximately 280,000 subscribers across the Island. Since April 1, 2015 up to the effective date of the new contract, TSS provided medical, mental, pharmacy and dental healthcare services to Medicaid subscribers in the Metro-North and West regions of the government of Puerto Rico's health insurance program, which included approximately 400,000 subscribers, on an at-risk basis.

A substantial majority of the Company's business activity is within Puerto Rico, and as such, the Company is subject to the risks associated with the Puerto Rico economy.

Triple-S Management Corporation and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

2. Significant Accounting Policies

The following are the significant accounting policies followed by the Company and its subsidiaries:

Basis of Presentation

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). The consolidated financial statements include the financial statements of the Company and its subsidiaries. Intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of the consolidated financial statements in conformity with GAAP requires the Company to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Cash Equivalents

The Company considers all highly liquid debt instruments with maturities of three months or less at the date of acquisition to be cash equivalents. Cash and cash equivalents are recorded at cost, which approximates fair value. Cash equivalents of \$49,233 and \$87,572 at December 31, 2018 and 2017, respectively, consist principally of money market funds and certificates of deposit with original maturities of three months or less.

Investments

Fixed maturities

Investment in debt securities at December 31, 2018 and 2017 consists mainly of obligations of government-sponsored enterprises, U.S. Treasury securities and obligations of U.S. government instrumentalities, obligations of the Commonwealth of Puerto Rico and its instrumentalities, municipal securities, corporate bonds, residential mortgage-backed securities, and collateralized mortgage obligations. The Company classifies its debt securities in one of two categories: available-for-sale or held-to-maturity. Securities classified as held-to-maturity are those securities in which the Company has the ability and intent to hold until maturity. All other securities not included in held-to-maturity are classified as available-for-sale.

Available-for-sale securities are recorded at fair value. The fair values of debt securities (both available-for-sale and held-to-maturity investments) are based on quoted market prices for those or similar investments at the reporting date. Held-to-maturity debt securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums and discounts, respectively. Unrealized holding gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are reported as a separate component of other comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are included in earnings and are determined on a specific-identification basis.

Transfers of securities between categories are recorded at fair value at the date of transfer. Unrealized holding gains or losses associated with transfers of securities from held-to-maturity to available-for-sale are recorded as a separate component of other comprehensive income. The unrealized holding gains or losses included in the separate component of other comprehensive income for securities transferred from available-for-sale to held-to-maturity, are maintained and

Triple-S Management Corporation and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

amortized into earnings over the remaining life of the security as an adjustment to yield in a manner consistent with the amortization or accretion of premium or discount on the associated security.

If a fixed maturity security is in an unrealized loss position and the Company has the intent to sell the fixed maturity security, or it is more likely than not that the Company will have to sell the fixed maturity security before recovery of its amortized cost basis, the decline in value is deemed to be other-than-temporary and is recorded to other-than-temporary impairment losses recognized in earnings in the Company's consolidated statements of earnings. For impaired fixed maturity securities that the Company does not intend to sell or it is more likely than not that such securities will not have to be sold, but the Company expects not to fully recover the amortized cost basis, the credit component of the other-than-temporary impairment is recognized in other-than-temporary impairment losses recognized in earnings in the Company's consolidated statements of earnings and the non-credit component of the other-than-temporary impairment is recognized in other comprehensive income. Furthermore, unrealized losses entirely caused by non-credit related factors related to fixed maturity securities for which the Company expects to fully recover the amortized cost basis continue to be recognized in accumulated other comprehensive income.

The credit component of an other-than-temporary impairment is determined by comparing the net present value of projected future cash flows with the amortized cost basis of the fixed maturity security. The net present value is calculated by discounting the Company's best estimate of projected future cash flows at the effective interest rate implicit in the fixed maturity security at the date of acquisition.

A decline in the fair value of any available-for-sale or held-to-maturity security below cost that is deemed to be other-than-temporary results in an impairment to reduce the carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. To determine whether an impairment is other-than-temporary, the Company considers whether it has the ability and intent to hold the investment until a market price recovery and considers whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the impairment, the severity and duration of the impairment, market conditions, changes in value subsequent to year-end, forecasted performance of the investee, and the general market condition in the geographic area or industry the investee operates in.

Premiums and discounts are amortized or accreted over the life of the related held-to-maturity or available-for-sale security as an adjustment to yield using the effective interest method. Dividend and interest income are recognized when earned.

The Company regularly invests in mortgaged-backed securities and other securities subject to prepayment and call risk. Significant changes in prevailing interest rates may adversely affect the timing and amount of cash flows on such securities. In addition, the amortization of market premium and accretion of market discount for mortgaged-backed securities is based on historical experience and estimates of future payment speeds on the underlying mortgage loans. Actual prepayment speeds may differ from original estimates and may result in material adjustments to amortization or accretion recorded in future periods.

Triple-S Management Corporation and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

Equity investments

Investment in equity securities at December 31, 2018 and 2017 consists of mutual funds whose underlying assets are comprised of domestic equity securities, international equity securities and higher risk fixed income instruments. Equity investments are recorded at fair value. The fair values of equity investments are mainly based on quoted market prices for those or similar investments at the reporting date. For a specific equity investment, the fair value is estimated using the net asset value (NAV) of the Company's ownership interest in the partnership. Following the implementation on January 1, 2018 of Accounting Standard Update (ASU) 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, unrealized holding gains and losses, on equity investments are included in earnings. Realized gains and losses from the sale of equity investments are included in earnings and are determined on a specific-identification basis.

Other invested assets

Other invested assets at December 31, 2018 and 2017 consist mainly of alternative investments in partnerships which invest in several private debt and private equity funds. Portfolios are diversified by vintage year, stage, geography, business sectors and number of investments. These investments are not redeemable with the funds. Distributions from each fund are received as the underlying investments of the funds are liquidated. It is estimated that the underlying assets of the funds will be liquidated in the next 5 to 12 years. The fair values of the investments in this class have been estimated using the net asset value (NAV) of the Company's ownership interest in the partnerships. Total unfunded capital commitments for these positions as of December 31, 2018 amounted to \$80,484. The remaining average commitments period is approximately three years.

Revenue Recognition

a. Managed Care

Subscriber premiums on the managed care business are billed in advance of their respective coverage period and the related revenue is recorded as earned during the coverage period. Managed care premiums are billed in the month prior to the effective date of the policy with a grace period of up to two months. If the insured fails to pay, the policy can be cancelled at the end of the grace period at the option of the Company.

Premiums for the Medicaid business are based on a bid contract with ASES and billed in advance of coverage period. Under the risk-based Medicaid contract that expired on October 31, 2018, there is an excess profit agreement which stipulates that the profit of TSS for each fiscal year of the contract term shall not exceed two and a half percentage (2.5%) of the fixed amount paid by ASES for each member. In the event that the profit exceeds this amount, TSS and ASES shall share the excess profit in proportions of fifty percent (50%), subject to the compliance by TSS with certain quality metrics. ASES retains the right to determine the outcome of the excess profit agreement that is based on audited financial statements of the contracted services submitted annually by TSS and the validation of the incurred-but-not-reported reserve by ASES's actuary. We estimate on a monthly basis any estimated amount due to ASES and reflect any adjustments to premium revenue in current operations. As the runout of the contract progresses and additional information becomes available, any change in the estimated accrual will be recorded in the operating results of the period in which the information becomes available. We report any estimated net amounts due to ASES within accounts payable and accrued liabilities in the consolidated balance sheets. As of December 31, 2018, the Company had accrued an estimated profit sharing due to ASES of \$4,294. There was no accrued profit sharing due to ASES as of December 31, 2017.

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The Medicaid contract that became effective November 1, 2018 includes a minimum medical loss ratio (MLR) provision where the Company has to remit to ASES the excess of the target MLR of 92% over the actual MLR for any given contract year and would be reflected as an adjustment to premium revenue in current operations. The target established in the contract follows regulation requirements of the Centers for Medicare and Medicaid Services (CMS) for Medicaid managed care contracts codified in 42 CFR part 438. As of December 31, 2018, there was no accrued amount due to ASES related to this provision.

Premiums for the Medicare Advantage (MA) business are based on a bid contract with CMS and billed in advance of the coverage period. We recognize premium revenue in the period in which we are obligated to provide services to our members. We record premiums earned but not received as premiums receivable and record premiums received in advance of the period of service as unearned premiums in the consolidated balance sheets. Unearned premiums are recognized as revenue throughout the related coverage period. MA contracts are renewed annually and provide for a risk factor to adjust premiums paid for members that represent a higher or lower risk to the Company. Retroactive rate adjustments are made periodically based on the aggregate health status and risk scores of the Company's MA membership. These risk adjustments are evaluated quarterly, based on actuarial estimates. Actual results could differ from these estimates. We recognize periodic changes to risk-adjusted premiums as revenue when the amounts are determinable and collection is reasonably assured, which is possible as additional diagnosis code information is reported to CMS, when the ultimate settlements are received from CMS, or we receive notification of such settlement amounts. The data provided to CMS to determine members' risk scores is subject to audit by CMS even after the annual settlements occur, which may result in the refund of premiums to CMS. As additional information becomes available, the recorded estimate is revised and reflected in operating results in the period in which it becomes available.

Prescription drug coverage is offered to Medicare eligible beneficiaries as part of MA plans (MA-PD). Premiums are based on a bid contract with CMS that considers the estimated costs of providing prescription drug benefits to enrolled participants. MA-PD premiums are subject to adjustment, positive or negative, based upon the application of risk corridors that compare the estimated prescription drug costs included in the bids to CMS to actual prescription drug costs. Variances exceeding certain thresholds may result in CMS making additional payments or in CMS requesting a refund for a portion of the premiums collected. The Company estimates and records adjustments to earned premiums related to estimated risk corridor payments based upon actual prescription drug costs for each reporting period as if the annual contract were to end at the end of each reporting period.

Administrative service fees include revenue from certain groups which have managed care contracts that provide for the group to be at risk for all or a portion of their claims experience. For these groups, the Company is not at risk and only handles the administration of managed care coverage for an administrative service fee. The Company pays claims under commercial self-funded arrangements from its own funds, and subsequently receives reimbursement from these groups. Claims paid under self-funded arrangements are excluded from the claims incurred in the accompanying consolidated financial statements. Administrative service fees under the self-funded arrangements are recognized based on the group's membership or incurred claims for the period multiplied by an administrative fee rate plus other fees. In addition, some of these self-funded groups purchase aggregate and/or specific stop-loss coverage. In exchange for a premium, the group's aggregate liability or the group's liability on any one episode of care is capped for the year. Premiums for the stop-loss coverage are actuarially

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determined based on experience and other factors and are recorded as earned over the period of the contract in proportion to the coverage provided. This fully insured portion of premiums is included within the premiums earned, net in the accompanying consolidated statements of earnings.

b. Life and Accident and Health Insurance

Premiums on life insurance policies are billed in advance of their respective coverage period and the related revenue is recorded as earned when due. Premiums on accident and health and other short-term policies are recognized as earned primarily on a pro rata basis over the contract period. Premiums on credit life policies are recognized as earned in proportion to the amounts of insurance in-force. Revenues from universal life and interest sensitive policies represent amounts assessed against policyholders, including mortality charges, surrender charges actually paid, and earned policy service fees. The revenues for limited payment contracts are recognized over the period that benefits are provided rather than on collection of premiums.

c. Property and Casualty Insurance

Premiums on property and casualty contracts are billed in advance of their respective coverage period and they are recognized as earned on a pro rata basis over the policy term. The portion of premiums related to the period prior to the end of coverage is recorded in the consolidated balance sheets as unearned premiums and is transferred to premium revenue as earned.

Allowance for Doubtful Receivables

The allowance for doubtful receivables is based on management's evaluation of the aging of accounts and such other factors which deserve current recognition, including the continued deterioration of the local economy, the exposure to government accounts, and the challenging business environment in the island. This evaluation is performed individually on larger accounts and includes the use of all available information such as the customer's credit worthiness and other relevant information. Actual losses could differ from these estimates. Receivables are charged-off against their respective allowance accounts when deemed to be uncollectible.

Deferred Policy Acquisition Costs and Value of Business Acquired

Certain direct costs of acquiring business in the life and accident and health, and property and casualty segments are deferred by the Company. Substantially all acquisition costs related to the managed care segment are expensed as incurred.

In the life and accident and health segment, deferred acquisition costs (DAC) consist of commissions and certain expenses related to the successful acquisition of the production of life, annuity, accident and health, and credit business. In the event that future premiums, in combination with policyholder reserves and anticipated investment income, could not provide for all future benefits and maintenance and settlement expenses, the amount of deferred policy acquisition costs would be reduced to provide for such amount. The related amortization is provided over the anticipated premium-paying period of the related policies in proportion to the ratio of annual premium revenue to expected total premium revenue to be received over the life of the policies. Interest is considered in the amortization of deferred policy acquisition cost and value of business acquired. For these contracts interest is considered at a level rate at the time of issue of each contract, from 3.90% to 5.75% for 2018 and 2017, and 5.15% for 2016, and, in the case of the value of business acquired, at the time of any acquisition.

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For certain other long-duration contracts, deferred amounts are amortized at historical and forecasted credited interest rates. Expected premium revenue is estimated by using the same mortality and withdrawal assumptions used in computing liabilities for future policy benefits. The method followed in computing deferred policy acquisition costs limits the amount of such deferred costs to their estimated net realizable value. In determining estimated net realizable value, the computations give effect to the premiums to be earned, related investment income, losses and loss-adjustment expenses, and certain other costs expected to be incurred as the premium is earned.

Costs deferred on universal life and interest sensitive products are amortized as a level percentage of the present value of estimated gross profits from investment yields, mortality, expenses and surrender charges. Estimates used are based on the Company's experience as adjusted to provide for possible adverse deviations. These estimates are periodically reviewed and compared with actual experience. When it is determined that future expected experience differs significantly from that assumed, the estimates are updated for current and future issues which may result in a change or release of deferred policy acquisition costs amortization through the consolidated statements of earnings.

The value assigned to the life insurance in-force at the date of the acquisition is amortized using methods similar to those used to amortize the deferred policy acquisition costs of the life and accident and health segment.

In the property and casualty segment, acquisition costs consist of commissions incurred during the production of business and are deferred and amortized ratably over the terms of the policies.

Property and Equipment

Property and equipment are stated at cost. Maintenance and repairs are expensed as incurred. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets. Costs of computer equipment, programs, systems, installations, and enhancements are capitalized and amortized straight-line over their estimated useful lives. The following is a summary of the estimated useful lives of the Company's property and equipment:

Asset Category	Estimated Useful Life
Buildings	20 to 50 years
Building improvements	3 to 10 years
Leasehold improvements	10 years
Office furniture	7 years
Computer software	3 to 5 years
Computer equipment, equipment, and automobiles	3 to 5 years

Long-Lived Assets, including Goodwill

Long-lived assets, such as property and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the

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carrying amount of the asset exceeds the fair value of the asset. The assets and liabilities of a disposal group classified as held for sale would be presented separately in the appropriate asset and liability sections of the consolidated balance sheets. During 2018, 2017 and 2016, impairment tests on intangible assets were performed and based on the results of the tests no impairment was recorded.

Goodwill and intangible assets that have indefinite useful lives are tested at least annually for impairment, and are tested for impairment more frequently if events or circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. For goodwill, the impairment determination is made at the reporting unit level. The Company may perform a qualitative analysis under certain circumstances, or perform a two-step quantitative analysis. In the qualitative analysis, the Company determines if it is more likely than not that the fair value of a reporting unit is less than its carrying amount by assessing current events and circumstances. If there are factors present indicating potential impairment, the Company would proceed to the two-step quantitative analysis. The two-step impairment test is used to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any). First, the Company determines the fair value of a reporting unit and compares it to its carrying amount. Second, if the carrying amount of a reporting unit exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill.

The annual impairment test is based on an evaluation of estimated future discounted cash flows. The Company also uses the market approach as part of their impairment analysis. The estimated discounted cash flows are based on the best information available, including supportable assumptions and projections we believe are reasonable. Our discounted cash flow estimates use discount rates that correspond to a weighted-average cost of capital consistent with a market-participant view. The discount rates are consistent with those used for investment decisions and take into account the operating plans and strategies of our operating segments. Certain other key assumptions utilized, including changes in membership, premium, health care costs, operating expenses, fees, assessments and taxes and effective tax rates, are based on estimates consistent with those utilized in our annual budgeting and planning process that we believe are reasonable. However, if we do not achieve the results reflected in the assumptions and estimates, our goodwill impairment evaluations could be adversely affected, and we may impair a portion of our goodwill, which would adversely affect our operating results in the period of impairment. Impairments, if any, would be classified as an operating expense.

Claim Liabilities

Managed care claim liabilities mostly represent the Company's estimate of medical costs incurred but not yet paid to providers based on experience and accumulated statistical data. Loss-adjustment expenses related to such claims are currently accrued based on estimated future expenses necessary to process such claims. Claim liabilities are the most significant estimate included in our consolidated financial statements. Such estimate is developed consistently using standard actuarial methodologies based upon key assumptions, which vary by business segment. The most significant assumptions used in the development of managed care claim liabilities include current payment experience, trend factors, and completion factors. Managed care trend factors in our standard actuarial methodologies include contractual requirements, historic utilization trends, the interval between the date services are rendered and the date claims are paid, denied claims activity, disputed

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claims activity, benefit changes, expected health care cost inflation, seasonality patterns, maturity of lines of business, changes in membership and other factors.

Managed care claim liabilities also include a provision for adverse deviation, which is an estimate for known environmental factors that are reasonably likely to affect the required level of reserves. This provision for adverse deviation is intended to capture the potential adverse development from known environmental factors such as our entry into new geographical markets, changes in our geographic or product mix, the introduction of new customer populations, variation in benefit utilization, disease outbreaks, changes in provider reimbursement, fluctuations in medical cost trend, variation in claim submission patterns and variation in claims processing speed and payment patterns, changes in technology that provide faster access to claims data or change the speed of adjudication and settlement of claims, variability in claim inventory levels, non-standard claim development, and/or exceptional situations that require judgmental adjustments in setting the reserves for claims.

The Company contracts with various independent practice associations (IPAs) for certain medical care services provided to certain policies subscribers. The IPAs are compensated on a capitation basis and capitation payables are included within claim liabilities. Capitation is amounts paid to the aforementioned IPAs on a fixed-fee per member per month basis.

Claim liabilities also include unpaid claims and loss-adjustment expenses of the life and accident and health segment based on a case-basis estimate for reported claims, and on estimates, based on experience, for unreported claims and loss-adjustment expenses. The liability for policy and contract claims and claims expenses has been established to cover the estimated net cost of insured claims.

Also included within the claim liabilities is the liability for losses and loss-adjustment expenses for the property and casualty segment which represents individual case estimates for reported claims and estimates for unreported losses, net of any salvage and subrogation based on past experience modified for current trends and estimates of expenses for investigating and settling claims.

Claim liabilities are necessarily based on estimates and, while management believes that the amounts are adequate, the ultimate liability may be in excess of or less than the amounts provided. The methods for making such estimates and for establishing the resulting liability are continually reviewed, and any adjustments are reflected in the consolidated statements of earnings in the period determined.

Future Policy Benefits

The liability for future policy benefits has been computed using the level-premium method based on estimated future investment yield, mortality, morbidity and withdrawal experience. Mortality has been calculated principally on select and ultimate tables in common usage in the industry. Withdrawals have been estimated principally based on industry tables, modified by Company's experience. Assumptions are established at the time the policy is issued and are generally not changed during the life of the policy. The Company periodically reviews the adequacy of reserves for these policies on an aggregate basis using actual experience. If actual experience is significantly adverse compared to the original assumptions and a premium deficiency is determined to exist, any remaining unamortized DAC balance would be expensed to the extent not recoverable and the establishment of a premium deficiency reserve may be required. The interest rate assumption ranges between 3.90% and 5.75% for all years in issue.

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Policyholder Deposits

Amounts received for annuity contracts are considered deposits and recorded as a liability along with the accrued interest and reduced for charges and withdrawals. Interest incurred on such deposits, which amounted to \$2,615, \$2,798, and \$3,182, during the years ended December 31, 2018, 2017, and 2016, respectively, is included within the interest expense in the accompanying consolidated statements of earnings.

Policyholder account balances for universal life and interest sensitive products are equal to policy account values. The policy account primarily comprises cumulative deposits received and interest credited to the policyholder less cumulative contract benefits, surrenders, withdrawals, maturities and contract charges for mortality or administrative expenses. Interest rates credited to policyholder account balances during 2018 and 2017 ranged from 2.0% to 4.5% for universal life and interest sensitive products. The universal life and interest sensitive products represented \$83,563 and \$75,956 of the policyholder deposits balance on the consolidated balance sheets as of December 31, 2018 and 2017, respectively.

Reinsurance

In the normal course of business, the insurance-related subsidiaries seek to limit their exposure that may arise from catastrophes or other events that cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers.

Prospective reinsurance premiums, commissions, and expense reimbursements, related to reinsured business are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Accordingly, reinsurance premiums are reported as prepaid reinsurance premiums and amortized over the remaining contract period in proportion to the amount of insurance protection provided.

Premiums ceded and recoveries of losses and loss-adjustment expenses under prospective reinsurance treaties have been reported as a reduction of premiums earned and losses and loss-adjustment expenses incurred, respectively. Property and casualty commission and expense allowances received in connection with reinsurance ceded have been accounted for as a reduction of the related policy acquisition costs and are deferred and amortized accordingly. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy and are presented within premium and other receivables, net in the accompanying consolidated balance sheets. Accounts payable and accrued liabilities within the accompanying consolidated balance sheets include \$2,712 and \$110,850 of advances received for hurricane related claims as of December 31, 2018 and 2017, respectively.

Retroactive reinsurance reimburses a ceding company for liabilities incurred as a result of past insurable events covered under contracts subject to the reinsurance. In certain instances, reinsurance contracts cover losses both on a prospective basis and on a retroactive basis and where practical the Company bifurcates the prospective and retrospective elements of these reinsurance contracts and accounts for each element separately. Initial gains in connection with retroactive reinsurance contracts are deferred and amortized into income over the settlement period while losses are recognized immediately. When changes in the estimated amount recoverable from the reinsurer or in the timing of receipts related to that amount occur, a cumulative amortization adjustment is recognized in earnings in the period of the change so that the deferred gain reflects the balance that would have existed had the revised estimate been available at the inception of the reinsurance transaction. The Company uses the recovery method to amortize any deferred gain, which is

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included within the claims incurred in the accompanying consolidated statements of earnings. The recovery method provides an amortization in proportion to the estimated recoveries made as of each reporting date as a percentage of total estimated recoveries.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the consolidated statements of earnings in the period that includes the enactment date. The Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in circumstances occurs.

The Company records any interest and penalties related to unrecognized tax benefits within the operating expenses in the consolidated statement of earnings.

Health Insurance Providers Fee

The Patient Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act mandates an annual Health Insurance Providers Fee (HIP Fee). The annual HIP Fee becomes payable to the U.S. Treasury once the entity provides health insurance for any U.S. health risk each applicable calendar year. The initial estimated annual fee is accrued as of January 1, with a corresponding deferred cost that is amortized over 12 months on a straight-line basis. The fee payment is due on September 30 of each year. The Company incurred approximately \$50,100 and \$44,100 of such fees in 2018 and 2016, respectively, which are presented within operating expenses in the accompanying consolidated statements of earnings. The HIP Fee was waived for all health insurance providers during the year ended December 31, 2017.

Insurance-Related Assessments

The Company records a liability for insurance-related assessments when the following three conditions are met: (1) the assessment has been imposed or the information available prior to the issuance of the consolidated financial statements indicates it is probable that an assessment will be imposed; (2) the event obligating an entity to pay (underlying cause of) an imposed or probable assessment has occurred on or before the date of the consolidated financial statements; and (3) the amount of the assessment can be reasonably estimated. A related asset is recognized when the paid or accrued assessment is recoverable through either premium taxes or policy surcharges.

Commitments and Contingencies

Liabilities for loss contingencies arising from claims, assessments, litigation, fines, and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. Legal costs incurred in connection with loss contingencies are expensed as incurred. Recoveries of costs from third parties, which are probable of realization, are separately recorded as assets, and are not offset against the related liability.

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Share-Based Compensation

Share-based compensation is measured at the fair value of the award and recognized as an expense in the consolidated financial statements over the vesting period.

Earnings per Share

Basic earnings per share excludes dilution and is computed by dividing net income available to all classes of common stockholders by the weighted average number of all classes of common shares outstanding for the period, excluding non-vested restricted stocks. Diluted earnings per share is computed in the same manner as basic earnings per share except that the number of shares is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares had been issued. Dilutive common shares are included in the diluted earnings per share calculation using the treasury stock method.

Recently Adopted Accounting Standards

On January 5, 2016, the FASB issued guidance to enhance the reporting model for financial instruments to provide users of financial statements with more decision-useful information (Accounting Standard Update (ASU) 2016-01). Among the many targeted improvements to U.S. GAAP are (1) requiring equity investments, except those accounted for under the equity method of accounting or those that result in consolidation of the investee, to be measured at fair value with changes in fair value recognized in net income; (2) simplifying the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (3) eliminating the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; and (4) clarifying that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. This guidance applies to all entities that hold financial assets or owe financial liabilities. The Company also adopted guidance issued by FASB on March 9, 2018 that removes the previous guidance for Other Than Temporary Impairment of Certain Investments in Equity Securities as required by SEC Staff Accounting Bulletin (SAB) No. 117 and SEC Release No. 33-9273, since it is no longer applicable. For public companies, these amendments became effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company adopted this guidance for equity securities effective January 1, 2018. A cumulative-effect adjustment of \$39,882 was made from accumulated other comprehensive income to the beginning retained earnings at the implementation date.

On February 28, 2018, the Financial Accounting Standard Board (FASB) issued guidance for Technical Corrections and Improvement to Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities. Areas for correction or improvement include (1) equity securities without a readily determinable fair value—discontinuation, (2) equity securities without a readily determinable fair value—adjustments, (3) forward contracts and purchased options, (4) presentation requirements for certain fair value option liabilities, (5) fair value option liabilities denominated in a foreign currency, and (6) transition guidance for equity securities without a readily determinable fair value. For public companies, these amendments, became effective on a prospective basis, for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For public entities with fiscal years beginning between December 15, 2017 and June 15, 2018 adoption of these amendments was not effective until the interim period beginning after June 15, 2018. The Company adopted this guidance effective June 30, 2018. The adoption of this guidance did not have a material impact on the presentation of the Company's consolidated results of operations.

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Future Adoptions of Accounting Standards

On February 25, 2016, the Financial Accounting Standards Board (FASB) issued guidance to increase transparency and comparability among organizations by requiring the recognition of a lease right-of-use (ROU) asset and a lease liability, initially measured at the present value of the lease payment on the balance sheet, for both finance and operating leases with lease terms of more than 12 months. The classification of finance or operating will determine whether lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease, respectively. Lessors are required to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. In July 2018, the FASB issued the following guidance “Leases – Targeted Improvements” and “Codification Improvement to Leases” to assist in the implementation of leases and address certain technical corrections and improvement to the recently issued lease standard. Amendments include an additional transition method that allows entities to apply the new standard on the adoption date and recognize a cumulative effect adjustment to the opening balance of retained earnings, as well as a new practical expedient for lessors and other implementation considerations. For public companies, the amended guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company will adopt the standard effective January 1, 2019 using a modified prospective approach by recording a cumulative effect adjustment to beginning retained earnings at the implementation date for leases existing as of that date. The Company does not expect the standard to have a material impact in its consolidated balance sheet following the recognition of ROU assets and lease liabilities for its operating leases. We do not expect the adoption of this guidance to have a material impact on our consolidated statement of earnings or cash flows. In addition, the Company implemented control processes and procedures, as necessary, based on changes resulting from the new standard.

On June 16, 2016, the FASB issued guidance to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date by replacing the incurred loss impairment methodology in current U.S. GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. For public companies, these amendments are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company does not expect a material impact from the implementation of this guidance.

On January 26, 2017, the FASB issued guidance to simplify the manner in which an entity is required to evaluate goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Instead, under the amendments in this guidance, an entity should (1) perform its annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount, and (2) recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value, with the understanding that the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. Additionally, this guidance removes the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails such qualitative test, to perform Step 2 of the goodwill impairment test. For public companies, these amendments, which should be applied on a prospective basis, are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years.

On July 16, 2018, the FASB issued guidance Codification Improvements which represents changes to clarify, correct errors in, or make minor improvements to the Codification. The change addresses conflicts or unclear intent in the following areas: (1) Comprehensive Income – Overall, (2) Debt – Modifications and Extinguishments, (3) Distinguishing Liabilities from Equity – Overall, (3) Compensation – Stock Compensation – Income Taxes, (4) Derivatives and Hedging – Overall –

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Other Presentation Matters, (5) Fair Value Measurement – Overall and (6) Financial Services – Brokers and Dealers – Liabilities and Financial Services – Depository and Lending. Some of the amendments in this update do not require transition guidance and are effective immediately. However, many of the amendments do have transition guidance, effective for public companies for annual periods beginning after December 15, 2018. The guidance will be implemented effective January 1, 2019. The Company does not expect a material impact from the implementation of this guidance.

On August 15, 2018, the FASB issued guidance for Financial Services – Insurance: Targeted Improvements to the Accounting for Long-Duration Contracts which provides meaningful improvements to the existing recognition, measurement, presentation, and disclosure requirements for long-duration contracts issued by an insurance entity. The amendments improve the timeliness of recognizing changes in the liability for future policy benefits for long-duration contracts by requiring that underlying cash flow assumptions are reviewed and updated at least annually to current estimates without a provision for adverse deviation. The resulting change to the liability for future policy benefits related to the assumption changes will be recognized within earnings. The discount rate used to discount future cash flows will be updated both annually and at each interim period based on the yield of an upper-medium grade fixed-income instrument. The resulting change in the liability for Future Policy Benefits will be reported through Other Comprehensive Income. The guidance also introduces a new concept for market risk benefits for certain contracts which protect the contract holder from other-than-normal capital market risk and which expose the insurance company to such risks. These contracts will be required to be measured at fair value with the corresponding changes in value reported through net income. Additionally, the amendment simplifies the amortization of deferred acquisition costs and other balances amortized in proportion to premiums, gross profits, or gross margins, and requires that those balances be amortized on a constant level basis over the expected term of the related contracts. This guidance also requires increased and enhanced disclosure requirements for long-duration contracts and related balances. For public companies, these amendments will be applied for fiscal years beginning after December 15, 2020. The Company is currently evaluating the impact the adoption of this guidance may have in its consolidated financial statements.

On August 27, 2018, the FASB issued guidance for Fair Value Measurement – Disclosure Framework – Changes to the Disclosure Requirement for Fair Value Measurement. This update focuses on improving the effectiveness of disclosures in the notes to the financial statements by facilitating clear communication of the information required by U.S. GAAP that is most important to users of each entity's financial statements. Specifically certain disclosure requirements are removed (the amount of, and reasons for, transfer between Level 1 and Level 2 of the fair value hierarchy; the policy for timing of transfers between levels; the valuation processes for Level 3 fair value measurements) while it modifies and adds certain other disclosures (the changes in unrealized gains and losses for the period included in other comprehensive income for recurring Level 3 fair value measurements held at the end of the reporting period, and the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements). The amendments regarding changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements, and the narrative description of measurement uncertainty should be applied prospectively for only the most recent period in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. For public companies, these amendments will be applied for fiscal years beginning after December 15, 2019. The adoption of this guidance should not have a material impact on the presentation of the Company's consolidated result of operations.

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On August 28, 2018, the FASB issued guidance for Compensation – Retirement Benefits – Defined Benefit Plans – General which addresses changes to the disclosure requirement for defined benefit plans. The amendments in this guidance modify the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. Specifically certain disclosure requirements are removed (i.e. the amounts of accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year, related party disclosures concerning the amount of future annual benefits covered by an insurance and annuity contracts and significant transactions between the employer and related parties and the plan) while certain other disclosures are added (i.e. the weighted-average interest crediting rates for cash balance plans and other plans with promised interest crediting rates, an explanation for the reasons for significant gains and losses related to changes in the benefit obligation for the period). For public companies, these amendments, will be applied for fiscal years beginning after December 15, 2020. The adoption of this guidance should not have a material impact on the presentation of the Company's consolidated result of operations.

On August 29, 2018, the FASB issued guidance for Intangibles – Goodwill and Other – Internal-Use Software. Guidance addresses customer's accounting for implemented costs incurred in a cloud computing arrangement that is a service contract and aims to reduce complexity in the accounting for costs of implementing a cloud computing service arrangement. The amendments require a customer in a hosting arrangement that is a service contract to determine which implementation costs to capitalize as an asset related to service contract and which costs to expense. Additionally, it requires the customer to expense the capitalized implementation costs over the term of the hosting arrangement. For public companies, these amendments, will be applied on a prospective basis, for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The adoption of this guidance should not have a material impact on the presentation of the Company's consolidated result of operations.

Other than the accounting pronouncements disclosed above, there were no other new accounting pronouncements issued during the year that could have a material impact on the Corporation's financial position, operating results or financials statement disclosures.

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3. Investment in Securities

The amortized cost for debt securities and cost for alternative investments, gross unrealized gains, gross unrealized losses, and estimated fair value for the Company's investments in securities by major security type and class of security as of December 31, were as follows:

	2018			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Fixed maturities available for sale				
Obligations of government- sponsored enterprises	\$ 21,470	\$ 120	\$ (1)	\$ 21,589
U.S. Treasury securities and obligations of U.S. government instrumentalities	174,675	2,349	-	177,024
Obligations of the Commonwealth of Puerto Rico and its instrumentalities	8,295	-	-	8,295
Municipal securities	692,205	18,112	(538)	709,779
Corporate bonds	186,085	9,724	(239)	195,570
Residential mortgage-backed securities	75,373	1,298	-	76,671
Collateralized mortgage obligations	10,266	208	-	10,474
Total fixed maturities available for sale	<u>\$ 1,168,369</u>	<u>\$ 31,811</u>	<u>\$ (778)</u>	<u>\$ 1,199,402</u>

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	2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities available for sale				
Fixed maturities				
Obligations of government- sponsored enterprises	\$ 1,431	\$ 13	\$ -	\$ 1,444
U.S. Treasury securities and obligations of U.S. government instrumentalities	118,858	41	(550)	118,349
Obligations of the Commonwealth of Puerto Rico and its instrumentalities	8,059	34	-	8,093
Municipal securities	771,789	30,468	(1,467)	800,790
Corporate bonds	217,046	17,767	(489)	234,324
Residential mortgage-backed securities	32,465	2	(355)	32,112
Collateralized mortgage obligations	22,003	10	(337)	21,676
Total fixed maturities	1,171,651	48,335	(3,198)	1,216,788
Equity securities				
Mutual Funds	292,459	50,072	(223)	342,308
Alternative investments	34,670	559	(244)	34,985
Total equity securities	327,129	50,631	(467)	377,293
Total	\$ 1,498,780	\$ 98,966	\$ (3,665)	\$ 1,594,081

	2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Fixed maturities held to maturity				
U.S. Treasury securities and obligations of U.S. government instrumentalities	\$ 617	\$ 125	\$ -	\$ 742
Residential mortgage-backed securities	190	2	-	192
Certificates of deposits	1,685	-	-	1,685
Total	\$ 2,492	\$ 127	\$ -	\$ 2,619

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	2017			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Securities held to maturity				
U.S. Treasury securities and obligations of U.S. government instrumentalities	\$ 617	\$ 154	\$ -	\$ 771
Residential mortgage-backed securities	191	2	-	193
Certificates of deposits	1,511	-	-	1,511
	<u>\$ 2,319</u>	<u>\$ 156</u>	<u>\$ -</u>	<u>\$ 2,475</u>

	2018			Estimated fair value
	Amortized cost	Gross unrealized gains	Gross unrealized losses	
Other invested assets - Alternative investments	\$ 72,627	\$ 2,042	\$ (654)	\$ 74,015

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Gross unrealized losses on investment securities and the estimated fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, were as follows:

	2018								
	Less than 12 months			12 months or longer			Total		
	Gross			Gross			Gross		
	Estimated Fair Value	Unrealized Loss	Number of Securities	Estimated Fair Value	Unrealized Loss	Number of Securities	Estimated Fair Value	Unrealized Loss	Number of Securities
Fixed maturities available for sale									
Obligations of government-sponsored enterprises	\$ 1,469	\$ (1)	1	\$ -	\$ -	-	\$ 1,469	\$ (1)	1
Municipal securities	62,328	(349)	10	17,648	(189)	3	79,976	(538)	13
Corporate bonds	52,539	(239)	18	-	-	-	52,539	(239)	18
Total fixed maturities	<u>\$116,336</u>	<u>\$ (589)</u>	<u>29</u>	<u>\$ 17,648</u>	<u>\$ (189)</u>	<u>3</u>	<u>\$ 133,984</u>	<u>\$ (778)</u>	<u>32</u>
Other invested assets - Alternative investments	\$ 7,399	\$ (351)	3	\$ 10,447	\$ (303)	2	\$ 17,846	\$ (654)	5

	2017								
	Less than 12 months			12 months or longer			Total		
	Gross			Gross			Gross		
	Estimated Fair Value	Unrealized Loss	Number of Securities	Estimated Fair Value	Unrealized Loss	Number of Securities	Estimated Fair Value	Unrealized Loss	Number of Securities
Securities available for sale									
Fixed maturities									
U.S. Treasury securities and obligations of U.S. governmental instrumentalities	\$ 96,617	\$ (550)	7	\$ -	\$ -	-	96,617	(550)	7
Municipal securities	162,731	(1,467)	27	-	-	-	162,731	(1,467)	27
Corporate bonds	80,374	(489)	16	-	-	-	80,374	(489)	16
Residential mortgage-backed securities	31,736	(355)	19	-	-	-	31,736	(355)	19
Collateralized mortgage obligations	13,630	(239)	3	7,294	(98)	2	20,924	(337)	5
Total fixed maturities	<u>\$385,088</u>	<u>\$ (3,100)</u>	<u>72</u>	<u>\$ 7,294</u>	<u>\$ (98)</u>	<u>2</u>	<u>\$ 392,382</u>	<u>\$ (3,198)</u>	<u>74</u>
Equity securities									
Mutual funds	42,983	(223)	6	-	-	-	42,983	(223)	6
Alternative investments	9,986	(212)	5	3,162	(32)	1	13,148	(244)	6
Total equity securities	<u>52,969</u>	<u>(435)</u>	<u>11</u>	<u>3,162</u>	<u>(32)</u>	<u>1</u>	<u>56,131</u>	<u>(467)</u>	<u>12</u>
Total for securities available for sale	<u>\$438,057</u>	<u>\$ (3,535)</u>	<u>83</u>	<u>\$ 10,456</u>	<u>\$ (130)</u>	<u>3</u>	<u>\$ 448,513</u>	<u>\$ (3,665)</u>	<u>86</u>

The Company regularly monitors and evaluates the difference between the amortized cost and estimated fair value of fixed maturity securities. For fixed maturity securities with a fair value below amortized cost, the process includes evaluating: (1) the length of time and the extent to which the estimated fair value has been less than amortized cost, (2) the financial condition, near-term and long-term prospects for the issuer, including relevant industry conditions and trends, and implications of rating agency actions, (3) the Company's intent to sell or the likelihood of a required sale prior to recovery, (4) the recoverability of principal and interest, and (5) other factors, as applicable. This process is not exact and requires further consideration of risks such as credit and interest rate risks. Consequently, if an investment's cost exceeds its estimated fair value solely due to changes in interest rates, other-than temporary impairment may not be appropriate.

Due to the subjective nature of the Company's analysis, along with the judgment that must be applied in the analysis, it is possible that the Company could reach a different conclusion whether or not to impair a security if it had access to additional information about the investee. Additionally, it is possible that the investee's ability to meet future contractual obligations may be different than what

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the Company determined during its analysis, which may lead to a different impairment conclusion in future periods.

If after monitoring and analyzing impaired securities, the Company determines that a decline in the estimated fair value of any available-for-sale or held-to-maturity security below cost is other-than-temporary, the carrying amount of the security is reduced to its fair value in accordance with current accounting guidance. The new cost basis of an impaired security is not adjusted for subsequent increases in estimated fair value. In periods subsequent to the recognition of an other-than-temporary impairment, the impaired security is accounted for as if it had been purchased on the measurement date of the impairment. The discount (or reduced premium) based on the new cost basis may be accreted into net investment income in future periods based on prospective changes in cash flow estimates, to reflect adjustments to the effective yield.

The Company's process for identifying and reviewing available for sale and other invested assets for other-than-temporary impairments during any quarter includes the following:

- Identification and evaluation of securities that have possible indications of other-than-temporary impairment, which includes an analysis of all investments with gross unrealized investment losses that represent 20% or more of their cost and all investments with an unrealized loss greater than \$100.
- For any securities with a gross unrealized investment loss we might review and evaluate investee's current financial condition, liquidity, near-term recovery prospects, implications of rating agency actions, the outlook for the business sectors in which the investee operates and other factors.
- Consideration of evidential matter, including an evaluation of factors or triggers that may or may not cause individual investments to qualify as having other-than-temporary impairments.
- Determination of the status of each analyzed security as other-than-temporary or not, with documentation of the rationale for the decision; and

The Company reviews the available for sale and other invested assets portfolios under the Company's impairment review policy. Given market conditions and the significant judgments involved, there is a continuing risk that declines in fair value may occur and material other-than-temporary impairments may be recorded in future periods. The Company from time to time may sell investments as part of its asset/liability management process or to reposition its investment portfolio based on current and expected market conditions.

Obligations of Government-Sponsored Enterprises and Municipal Securities: The unrealized losses of these securities were mainly caused by fluctuations in interest rates and general market conditions. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the par value of the investment. In addition, these investments have investment grade ratings. Because the decline in fair value is attributable to changes in interest rates and not credit quality; because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity; and because the Company expects to collect all contractual cash flows, these investments are not considered other-than-temporarily impaired.

Corporate Bonds: The unrealized losses of these bonds were principally caused by fluctuations in interest rates and general market conditions. All corporate bonds with an unrealized loss have investment grade ratings. Because the decline in estimated fair value is principally attributable to changes in interest rates; because the Company does not intend to sell the investments and it is not

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more likely than not that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity; and because the Company expects to collect all contractual cash flows, these investments are not considered other-than-temporarily impaired.

Alternative Investments: As of December 31, 2018, alternative investments with unrealized losses are not considered other-than-temporarily impaired based on market conditions and the length of time the funds have been in a loss position.

Maturities of investment securities classified as available for sale and held to maturity at December 31, 2018 were as follows:

	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Securities available for sale		
Due in one year or less	\$ 18,707	\$ 18,809
Due after one year through five years	355,334	357,777
Due after five years through ten years	428,212	435,669
Due after ten years	280,477	300,002
Residential mortgage-backed securities	75,373	76,671
Collateralized mortgage obligations	10,266	10,474
	<u>\$ 1,168,369</u>	<u>\$ 1,199,402</u>
Securities held to maturity		
Due in one year or less	\$ 1,685	\$ 1,685
Due after ten years	617	742
Residential mortgage-backed securities	190	192
	<u>\$ 2,492</u>	<u>\$ 2,619</u>

Expected maturities may differ from contractual maturities because some issuers have the right to call or prepay obligations with or without call or prepayment penalties.

Investments with an amortized cost of \$7,982 and \$5,229 (fair value of \$8,217 and \$5,571) at December 31, 2018 and 2017, respectively, were deposited with the Commissioner of Insurance to comply with the deposit requirements of the Insurance Code of the Commonwealth of Puerto Rico (the Insurance Code).

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4. Realized and Unrealized Gains

Information regarding realized and unrealized gains and losses from investments for the years ended December 31, is as follows:

	2018	2017	2016
Realized gains (losses)			
Fixed maturity securities:			
Securities available for sale			
Gross gains	\$ 3,730	\$ 1,460	\$ 3,086
Gross losses	(18,627)	(2,176)	(2,744)
Total fixed maturity securities	(14,897)	(716)	342
Equity investments:			
Gross gains	16,045	12,154	19,674
Gross losses	(2,290)	(558)	(1,203)
Gross losses from other-than-temporary impairments	-	(49)	(1,434)
Total equity investments	13,755	11,547	17,037
Other invested assets:			
Gross gains	1,492	-	-
Gross losses	(52)	-	-
Total other invested assets	1,440	-	-
Net realized gains on securities	\$ 298	\$ 10,831	\$ 17,379
	2018	2017	2016
Changes in unrealized gains (losses)			
Recognized in accumulated other comprehensive income (loss)			
Fixed maturities – available for sale	\$ (14,104)	\$ (2,203)	\$ 1,953
Other invested assets	1,073	-	-
Equity securities	-	20,514	2,172
Not recognized in the consolidated financial statements			
Fixed maturities – held to maturity	\$ (29)	\$ (20)	\$ (19)

The change in deferred tax asset (liability) on unrealized gains (losses) recognized in accumulated other comprehensive income during the years 2018, 2017, and 2016 was \$2,292, \$(3,846), and \$(1,085), respectively.

As of December 31, 2018 and 2017 no individual investment in securities exceeded 10% of stockholders' equity.

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5. Net Investment Income

Interest and/or dividend income for the years ended December 31 were are as follows:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Fixed maturities	\$ 43,873	\$ 38,414	\$ 37,139
Equity securities	12,261	10,728	9,666
Other invested assets	1,679	-	-
Policy loans	754	709	619
Cash equivalents and interest-bearing deposits	1,407	798	257
Other	1,935	966	1,232
Total	<u>\$ 61,909</u>	<u>\$ 51,615</u>	<u>\$ 48,913</u>

6. Premium and Other Receivables, Net

Premium and other receivables, net as of December 31 were as follows:

	<u>2018</u>	<u>2017</u>
Premium	\$ 94,613	\$ 103,027
Self-funded group receivables	31,184	39,859
FEHBP	14,030	13,346
Agent balances	30,224	32,818
Accrued interest	12,426	14,331
Reinsurance recoverable	399,202	661,679
Other	88,807	70,150
	<u>670,486</u>	<u>935,210</u>
Less allowance for doubtful receivables:		
Premium	32,487	26,490
Other	9,555	9,393
	<u>42,042</u>	<u>35,883</u>
Premium and other receivables, net	<u>\$ 628,444</u>	<u>\$ 899,327</u>

As of December 31, 2018 and 2017, the Company had premiums and other receivables of \$54,329 and \$81,838, respectively, from the Government of Puerto Rico, including its agencies, municipalities and public corporations. The related allowance for doubtful receivables as of December 31, 2018 and 2017 were \$20,984 and \$16,436, respectively.

Reinsurance recoverable as of December 31, 2018 and 2017 includes \$350,353 and \$613,000 related to expected catastrophe losses covered by the Property and Casualty segment's reinsurance program, reflecting the anticipated gross losses related to Hurricanes Irma and Maria, which made landfall in Puerto Rico during the month of September 2017.

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7. Deferred Policy Acquisition Costs and Value of Business Acquired

The movement of deferred policy acquisition costs (DPAC) and value of business acquired (VOBA) for the years ended December 31 is summarized as follows:

	<u>DPAC</u>	<u>VOBA</u>	<u>Total</u>
Balance, December 31, 2015	\$ 161,731	\$ 28,917	\$ 190,648
Additions	47,742	-	47,742
VOBA interest at an average rate of 5.15%	-	1,381	1,381
Amortization	(40,848)	(4,136)	(44,984)
Net change	6,894	(2,755)	4,139
Balance, December 31, 2016	168,625	26,162	194,787
Additions	48,701	-	48,701
VOBA interest at an average rate of 5.17%	-	1,253	1,253
Amortization	(39,605)	(4,348)	(43,953)
Net change	9,096	(3,095)	6,001
Balance, December 31, 2017	177,721	23,067	200,788
Additions	51,144	-	51,144
VOBA interest at an average rate of 5.11%	-	1,120	1,120
Amortization	(35,005)	(2,888)	(37,893)
Net change	16,139	(1,768)	14,371
Balance, December 31, 2018	\$ 193,860	\$ 21,299	\$ 215,159

A portion of the amortization of the DPAC and VOBA is recorded as an amortization expense and included within the operating expenses in the accompanying consolidated statements of earnings. The remaining portion of the DPAC and VOBA amortization includes the unrealized investment gains and losses that would have been amortized if such gains and losses had been realized, which for the years ended December 31, 2018 and 2017 amounted to \$2,113 and \$598, respectively, and is included within the unrealized gains on securities component of other comprehensive income.

The estimated amount of the year-end VOBA balance expected to be amortized during the next five years is as follows:

Year ending December 31:	
2019	\$ 2,939
2020	2,064
2021	1,845
2022	1,630
2023	1,697

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8. Property and Equipment, Net

Property and equipment, net as of December 31 are composed of the following:

	<u>2018</u>	<u>2017</u>
Land	\$ 10,976	\$ 10,976
Buildings and leasehold improvements	68,424	64,856
Office furniture and equipment	39,421	35,070
Computer equipment and software	137,183	116,244
Automobiles	795	701
	<u>256,799</u>	<u>227,847</u>
Less accumulated depreciation and amortization	174,876	153,131
Property and equipment, net	<u>\$ 81,923</u>	<u>\$ 74,716</u>

The Company recognized depreciation expense on property and equipment of \$12,583, \$11,930, and \$12,335 for the years ended December 31, 2018, 2017, and 2016, respectively.

9. Goodwill

Certain business combination transactions have resulted in goodwill, which represents the excess of the acquisition cost over the fair value of net assets acquired, and is assigned to reporting units. Goodwill recorded as of December 31, 2018 and 2017 was \$25,397 which is all attributable to the Medicare Advantage reporting unit within the Managed Care segment.

As required by accounting guidance, the 2018, 2017 and 2016 annual goodwill impairment tests were performed, and based on the results of the tests, no impairment charge was required. If the Company does not achieve its earnings objectives or the cost of capital raises significantly, the assumptions and estimates underlying these impairment tests could be adversely affected and result in future impairment charges that would negatively impact its operating results. Cumulative goodwill impairment charges were \$2,369 as of December 31, 2018 and 2017. All cumulative goodwill impairment is related to the health clinic reporting unit which has been fully impaired.

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10. Fair Value Measurements

Assets recorded at fair value in the consolidated balance sheets are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Level inputs, as defined by current accounting guidance for fair value measurements and disclosures, are as follows:

Level Input Definition:

- | | |
|---------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Level 1 | Inputs are unadjusted, quoted prices for identical assets or liabilities in active markets at the measurement date. |
| Level 2 | Inputs other than quoted prices included in Level 1 that are observable for the asset or liability through corroboration with market data at the measurement date. |
| Level 3 | Unobservable inputs that reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. |

The Corporation uses observable inputs when available. Fair value is based upon quoted market prices when available. The Corporation limits valuation adjustments to those deemed necessary to ensure that the security's fair value adequately represents the price that would be received or paid in the marketplace. Valuation adjustments may include consideration of counterparty credit quality and liquidity as well as other criteria. The estimated fair value amounts are subjective in nature and may involve uncertainties and matters of significant judgment for certain financial instruments. Changes in the underlying assumptions used in estimating fair value could affect the results. The fair value measurement levels are not indicative of risk of investment.

Transfers into or out of the Level 3 category occur when unobservable inputs, such as the Company's best estimate of what a market participant would use to determine a current transaction price, become more or less significant to the fair value measurement. Transfers between levels, if any, are recorded as of the actual date of the event or change in circumstance that caused the transfer. There were no transfers between Levels 1 and 2 during the years ended December 31, 2018 and 2017.

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A reconciliation of the beginning and ending balances of assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31 is as follows:

Fair Value Measurements Using Significant Unobservable Inputs (Level 3)

	<u>2018</u>
Balance as of January 1,	\$ -
Realized gains	-
Unrealized in other accumulated comprehensive income	-
Purchases	3,805
Sales	-
Capital Distributions	-
Balance as of December 31,	<u>\$ 3,805</u>

The fair value of investment securities is estimated based on quoted market prices for those or similar investments. Additional information pertinent to the estimated fair value of investment in securities is included in note 3.

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The following table summarizes fair value measurements by level at December 31, for assets measured at fair value on a recurring basis:

	2018			
	Level 1	Level 2	Level 3	Total
Fixed maturity securities available for sale				
Obligations of government-sponsored enterprises	\$ -	\$ 21,589	\$ -	\$ 21,589
U.S. Treasury securities and obligations of U.S. government instrumentalities	177,024	-	-	177,024
Obligations of the Commonwealth of Puerto Rico and its instrumentalities	-	8,295	-	8,295
Municipal securities	-	709,779	-	709,779
Corporate bonds	-	195,570	-	195,570
Residential agency mortgage-backed securities	-	76,671	-	76,671
Collateralized mortgage obligations	-	10,474	-	10,474
Total fixed maturities	<u>\$ 177,024</u>	<u>\$ 1,022,378</u>	<u>\$ -</u>	<u>\$ 1,199,402</u>
Equity investments	<u>\$ 147,348</u>	<u>\$ 128,011</u>	<u>\$ 3,805</u>	<u>\$ 279,164</u>
	2017			
	Level 1	Level 2	Level 3	Total
Securities available for sale				
Fixed maturity securities				
Obligations of government-sponsored enterprises	\$ -	\$ 1,444	\$ -	\$ 1,444
U.S. Treasury securities and obligations of U.S. government instrumentalities	118,349	-	-	118,349
Obligations of the Commonwealth of Puerto Rico and its instrumentalities	-	8,093	-	8,093
Municipal securities	-	800,790	-	800,790
Corporate bonds	-	234,324	-	234,324
Residential agency mortgage-backed securities	-	32,112	-	32,112
Collateralized mortgage obligations	-	21,676	-	21,676
Total fixed maturities	<u>\$ 118,349</u>	<u>\$ 1,098,439</u>	<u>\$ -</u>	<u>\$ 1,216,788</u>
Equity securities	<u>\$ 193,159</u>	<u>\$ 149,149</u>	<u>\$ -</u>	<u>\$ 342,308</u>

The fair value of fixed maturity and equity securities included in the Level 2 category were based on market values obtained from independent pricing services, which use previously evaluated pricing models that vary by asset class and incorporate available trade, bid and other market information and for structured securities, cash flow and when available loan performance data. Because many fixed income securities do not trade on a daily basis, the models used by independent pricing service providers to prepare evaluations apply available information, such as benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing. For certain equity securities, quoted market prices for the identical security are not always available and the fair value is estimated by reference to similar securities for which quoted prices are available. The independent pricing service providers monitor market indicators, industry and economic events, and for broker-quoted only securities, obtain quotes from market makers or broker-dealers that they recognize to be market participants.

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In addition to the preceding disclosures on assets recorded at fair value in the consolidated balance sheets, accounting guidance also requires the disclosure of fair values for certain other financial instruments for which it is practicable to estimate fair value, whether or not such values are recognized in the consolidated balance sheets.

Non-financial instruments such as property and equipment, other assets, deferred income taxes and intangible assets, and certain financial instruments such as claim liabilities are excluded from the fair value disclosures. Therefore, the fair value amounts cannot be aggregated to determine our underlying economic value.

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, receivables, accounts payable and accrued liabilities, and short-term borrowings approximate fair value because of the short-term nature of these items. These assets and liabilities are not listed in the table below.

The following methods, assumptions and inputs were used to estimate the fair value of each class of financial instrument:

(i) Policy Loans

Policy loans have no stated maturity dates and are part of the related insurance contract. The carrying amount of policy loans approximates fair value because their interest rate is reset periodically in accordance with current market rates.

(ii) Policyholder Deposits

The fair value of policyholder deposits is the amount payable on demand at the reporting date, and accordingly, the carrying value amount approximates fair value.

(iii) Long-term Borrowings

The carrying amount of the loans payable to bank – variable approximates fair value due to its floating interest-rate structure. The fair value of the loans payable to bank – fixed and senior unsecured notes payable was determined using broker quotations.

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A summary of the carrying value and fair value by level of financial instruments not recorded at fair value on our consolidated balance sheets at December 31 are as follows:

	2018				
	Carrying	Fair Value			
	Value	Level 1	Level 2	Level 3	Total
Assets:					
Policy loans	\$ 9,469	\$ -	\$ 9,469	\$ -	\$ 9,469
Liabilities:					
Policyholder deposits	\$ 174,110	\$ -	\$ 174,110	\$ -	\$ 174,110
Long-term borrowings:					
Loans payable to bank - variable	29,114	-	29,114	-	29,114
Total liabilities	<u>\$ 203,224</u>	<u>\$ -</u>	<u>\$ 203,224</u>	<u>\$ -</u>	<u>\$ 203,224</u>
2017					
	Carrying	Fair Value			
	Value	Level 1	Level 2	Level 3	Total
Assets:					
Policy loans	\$ 9,077	\$ -	\$ 9,077	\$ -	\$ 9,077
Liabilities:					
Policyholder deposits	\$ 176,534	\$ -	\$ 176,534	\$ -	\$ 176,534
Long-term borrowings:					
Loans payable to bank - variable	32,350	-	32,350	-	32,350
Total liabilities	<u>\$ 208,884</u>	<u>\$ -</u>	<u>\$ 208,884</u>	<u>\$ -</u>	<u>\$ 208,884</u>

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11. Claim Liabilities and Claim Adjustment Expenses

A reconciliation of the beginning and ending balances of claim liabilities in 2018, 2017 and 2016 is as follows:

	2018		Consolidated
	Managed Care	Other Business Segments *	
Claim liabilities at beginning of year	\$ 367,357	\$ 739,519	\$ 1,106,876
Reinsurance recoverable on claim liabilities	-	(633,099)	(633,099)
Net claim liabilities at beginning of year	<u>367,357</u>	<u>106,420</u>	<u>473,777</u>
Claims incurred			
Current period insured events	2,308,516	103,368	2,411,884
Prior period insured events	(36,015)	120,961	84,946
Total	<u>2,272,501</u>	<u>224,329</u>	<u>2,496,830</u>
Payments of losses and loss-adjustment expenses			
Current period insured events	1,982,372	57,260	2,039,632
Prior period insured events	263,260	46,469	309,729
Total	<u>2,245,632</u>	<u>103,729</u>	<u>2,349,361</u>
Net claim liabilities at end of year	394,226	227,020	621,246
Reinsurance recoverable on claim liabilities	-	315,543	315,543
Claim liabilities at end of year	<u>\$ 394,226</u>	<u>\$ 542,563</u>	<u>\$ 936,789</u>

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	2017		
	Managed Care	Other Business Segments *	Consolidated
Claim liabilities at beginning of year	\$ 349,047	\$ 138,896	\$ 487,943
Reinsurance recoverable on claim liabilities	-	(38,998)	(38,998)
Net claim liabilities at beginning of year	<u>349,047</u>	<u>99,898</u>	<u>448,945</u>
Claims incurred			
Current period insured events	2,231,052	118,012	2,349,064
Prior period insured events	(12,782)	(8,975)	(21,757)
Total	<u>2,218,270</u>	<u>109,037</u>	<u>2,327,307</u>
Payments of losses and loss-adjustment expenses			
Current period insured events	1,940,410	64,051	2,004,461
Prior period insured events	259,550	38,536	298,086
Total	<u>2,199,960</u>	<u>102,587</u>	<u>2,302,547</u>
Net claim liabilities at end of year	367,357	106,348	473,705
Reinsurance recoverable on claim liabilities	-	633,171	633,171
Claim liabilities at end of year	<u>\$ 367,357</u>	<u>\$ 739,519</u>	<u>\$ 1,106,876</u>

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	2016		
	Managed Care	Other Business Segments *	Consolidated
Claim liabilities at beginning of year	\$ 348,297	\$ 143,468	\$ 491,765
Reinsurance recoverable on claim liabilities	-	(40,714)	(40,714)
Net claim liabilities at beginning of year	<u>348,297</u>	<u>102,754</u>	<u>451,051</u>
Claims incurred			
Current period insured events	2,356,594	103,049	2,459,643
Prior period insured events	(9,047)	(7,157)	(16,204)
Total	<u>2,347,547</u>	<u>95,892</u>	<u>2,443,439</u>
Payments of losses and loss-adjustment expenses			
Current period insured events	2,083,552	58,091	2,141,643
Prior period insured events	263,245	40,657	303,902
Total	<u>2,346,797</u>	<u>98,748</u>	<u>2,445,545</u>
Net claim liabilities at end of year	349,047	99,898	448,945
Reinsurance recoverable on claim liabilities	-	38,998	38,998
Claim liabilities at end of year	<u>\$ 349,047</u>	<u>\$ 138,896</u>	<u>\$ 487,943</u>

* Other Business Segments include the Life Insurance and Property and Casualty segments, as well as intersegment eliminations.

The actual amounts of claims incurred in connection with insured events occurring in a prior period typically differ from estimates of such claims made in the prior period. Amounts included as incurred claims for prior period insured events reflect the aggregate net amount of these differences.

The unfavorable developments in the claims incurred and loss-adjustment expenses for prior period insured events in 2018 is driven by an adverse development of approximately \$128,678 in the Property and Casualty segment losses related to Hurricane Maria, partially offset by better than expected utilization trends in the Managed Care segment. The favorable developments in the claims incurred and loss-adjustment expenses for prior period insured events for 2017 and 2016 are primarily due to better than expected utilization trends in the Managed Care segment. Reinsurance recoverable on unpaid claims is reported within the premium and other receivables, net in the accompanying consolidated financial statements.

The claims incurred disclosed in this table exclude the portion of the change in the liability for future policy benefits amounting to \$30,783, \$25,794, and \$28,752 that is included within the consolidated claims incurred during the years ended December 31, 2018, 2017 and 2016, respectively.

The following is information about incurred and paid claims development, net of reinsurance, as of December 31, 2018, as well as cumulative claim frequency. Additional information presented includes total incurred-but-not-reported liabilities plus expected development on reported claims is included within the net incurred claims amounts.

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The information about incurred and paid claims development for the year ended December 31, 2015 and previous years are presented as supplementary information and are unaudited where indicated. The average annual percentage payout of incurred claims by age as of December 31, 2018, is presented as required supplementary information.

Managed Care

The Company estimates its liabilities for unpaid claims following a detailed actuarial process that entails using both historical claim payment patterns as well as emerging medical cost trends to project a best estimate of claim liabilities. This process includes comparing the historical claims incurred dates to the actual dates on claims payment. Completion factors are applied to claims paid through the consolidated financial statements date to estimate the claim expense incurred for the current period. The liability for claim adjustment expenses consists of adjustments made by our actuaries based on their knowledge and their estimate of emerging impacts to benefit costs and payment speed.

Incurring Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance			As of December 31, 2018		
Incurring Year	2017	2018	Total of IBNR Liabilities Plus Expected Development on Reported Claims	(in thousands)	
				Cumulative Number of Reported Claims	
2017	\$ 2,231,052	2,216,578	65,459	17,652	
2018		2,308,516	325,857	18,259	
		Total			
		\$ 4,525,094			

Cumulative Paid Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance		
Incurring Year	2017	2018
2017	\$ 1,940,410	2,151,406
2018		1,982,372
		Total
		\$ 4,133,778
		All outstanding liabilities before 2017, net of reinsurance
		2,910
		Liabilities for claims and claim adjustment expenses, net of reinsurance
		\$ 394,226

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Property and Casualty

Claims liability for property and casualty represents individual case estimates for reported claims and estimates for unreported losses, net of any salvage and subrogation based on past experience modified for current trends and estimates of expense for investigating and setting claims.

All Lines

in thousands

Incurred Year	Incurred Claims and Allocated Claim Adjustment Expenses, Net of Reinsurance										As of December 31, 2018		
	Incurred amount										Total of IBNR Plus Expected Development on Reported Claims	Cumulative Number of reported claims	
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)			
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018			
2009	51,778	51,760	50,848	51,298	51,564	51,315	51,485	51,293	51,563	\$ 51,439	\$	99	16,089
2010		54,226	54,090	55,266	56,400	57,115	57,386	57,242	56,960	56,981		135	18,012
2011			51,315	50,287	51,105	50,776	51,895	52,099	51,729	51,684		168	20,919
2012				49,040	49,856	48,900	49,817	48,945	48,186	47,731		392	20,217
2013					52,343	51,030	49,606	49,168	48,229	47,550		785	22,360
2014						48,430	45,410	43,707	42,547	41,457		916	22,044
2015							45,067	40,175	37,271	35,505		1,094	20,069
2016								48,127	44,294	41,168		2,788	19,397
2017									60,694	187,376		15,519	47,415
2018										40,619		15,563	15,876
										Total	\$		601,510

Incurred Year	Cumulative Paid claims and Allocated Claim Adjustment Expenses, Net of Reinsurance										
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	
2009	23,843	35,327	41,810	45,838	48,637	49,709	50,196	50,371	50,594	\$ 50,680	
2010		27,118	38,964	45,409	49,808	52,890	54,027	54,996	55,715	56,253	
2011			24,534	34,835	41,606	44,996	47,908	49,598	50,457	50,761	
2012				22,677	33,620	40,406	43,663	45,607	46,094	46,441	
2013					21,376	33,249	38,979	42,840	44,252	45,234	
2014						18,752	28,657	33,809	36,875	37,857	
2015							17,063	24,935	28,040	30,729	
2016								20,099	28,996	32,820	
2017									28,414	41,855	
2018										16,555	
										\$ 409,185	
										All outstanding liabilities before 2009, net of reinsurance	1,623
										Liabilities for claims and claims adjustment expenses, net of reinsurance	\$ 193,948

The following table includes the annual percentage payout of incurred claims by age, net of reinsurance, for property and casualty segment as supplementary information as of December 31, 2018:

	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Average	43.2%	20.6%	11.7%	7.4%	4.3%	2.1%	1.3%	0.7%	0.7%	0.2%

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The reconciliation of the net incurred and paid claims development tables, by segment, to the liability for claims and claim adjustment expenses in the consolidated balance sheets is as follows:

	As of December 31, 2018	
Net outstanding liabilities		
Managed Care	\$	394,226
Property and Casualty		193,948
Other short-duration insurance lines		3,655
Liabilities for unpaid claims and claim adjustment expenses, net of reinsurance		<u>591,829</u>
Reinsurance recoverable on unpaid claims - Property and Casualty		<u>302,928</u>
Insurance lines other than short-duration		42,502
Intersegment elimination		(470)
Total gross liability for unpaid claims and claim adjustment expense	\$	<u><u>936,789</u></u>

Claim liabilities as of December 31, 2018 and 2017 include approximately \$415,900 and \$605,200, respectively, of gross losses related to the impact of Hurricanes Irma and Maria which made landfall in Puerto Rico in September 2017.

12. Federal Employees' Health Benefits (FEHBP) and Federal Employees' (FEP) Programs

FEHBP

In prior years, TSS entered into a contract, renewable annually, with the Office of Personnel Management (OPM) as authorized by the Federal Employees' Health Benefits Act of 1959, as amended, to provide health benefits under the FEHBP. The FEHBP covers postal and federal employees residing in the Commonwealth of Puerto Rico and the USVI as well as retirees and eligible dependents. The FEHBP is financed through a negotiated contribution made by the federal government and employees' payroll deductions.

The accounting policies for the FEHBP are the same as those described in the Company's summary of significant accounting policies. Premium rates are determined annually by TSS and approved by the federal government. Claims are paid to providers based on the guidelines determined by the federal government. Operating expenses are allocated from TSS's operations to the FEHBP based on applicable allocation guidelines (such as, the number of claims processed for each program) and are subject to contractual expense limitations.

The operations of the FEHBP do not result in any excess or deficiency of revenue or expense as this program has a special account available to compensate any excess or deficiency on its operations to the benefit or detriment of the federal government. Any transfer to/from the special account necessary to cover any excess or deficiency in the operations of the FEHBP is recorded as a reduction/increment to the premiums earned. The contract with OPM provides that the cumulative excess of the FEHBP earned income over health benefits charges and expenses represents a

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restricted fund balance denoted as the special account. Upon termination of the contract and satisfaction of all the FEHBP's obligations, any unused remainder of the special reserve would revert to the Federal Employees Health Benefit Fund. In the event that the contract terminates and the special reserve is not sufficient to meet the FEHBP's obligations, the FEHBP contingency reserve will be used to meet such obligations. If the contingency reserve is not sufficient to meet such obligations, the Company is at risk for the amount not covered by the contingency reserve.

The contract with OPM allows for the payment to the Company of service fees as negotiated between TSS and OPM.

The Company also has funds available related to the FEHBP amounting to \$60,959 and \$68,425 as of December 31, 2018 and 2017, respectively, and are included within cash and cash equivalents in the accompanying consolidated balance sheets. Such funds are used to cover health benefits charges, administrative expenses and service charges required by the FEHBP.

A contingency reserve is maintained by the OPM at the U.S. Treasury, and is available to the Company under certain conditions as specified in government regulations. Accordingly, such reserve is not reflected in the consolidated balance sheets. The balance of such reserve as of December 31, 2018 and 2017 was \$62,911 and \$32,928, respectively. The Company received \$27 and \$6,687, of payments made from the contingency reserve fund of OPM during 2017 and 2016, respectively. The Company did not receive contingency reserve payments during 2018. During the year ended December 31, 2018 the Company returned excess reserves of \$23,030 to the contingency reserve fund.

The claim payments and operating expenses charged to the FEHBP are subject to audit by the U.S. government. Management is of the opinion that an adjustment, if any, resulting from such audits will not have a significant effect on the accompanying consolidated financial statements. The claim payments and operating expenses reimbursed in connection with the FEHBP have been audited through 2011 by OPM.

FEP

In prior years, TSS entered into a contract with the BCBSA as per Contract No. C.S. 1039 with OPM to provide health benefits under one Government-wide Service Benefit Plan as contemplated in Title 5, Chapter 89, United States Code. The FEP covers employees and annuitants residing in the Commonwealth of Puerto Rico and the USVI as well as eligible dependents. The FEP is financed through a negotiated contribution made by the federal government and employees' payroll deductions. The accounting methodology and operations of the FEP are similar to those of the FEHBP as described before.

The claims payments and operating expenses charged to the FEP are subject to audit by the BCBSA. Management is of the opinion that the adjustments, if any, resulting from such audits will not have a significant effect in the accompanying consolidated financial statements. Operating expenses reimbursed in connection with the FEP have been audited through 2013 by BCBSA.

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13. Long-Term Borrowings

A summary of the borrowings entered by the Company as of December 31 is as follows:

	<u>2018</u>	<u>2017</u>
Secured loan payable of \$11,187, payable in monthly installments of \$137 through October 1, 2023, plus interest at a rate reset periodically of 100 basis points over selected LIBOR maturity (which was 3.35% at December 31, 2018).	\$ 7,907	\$ 9,547
Secured loan payable of \$20,150, payable in monthly installments of \$84 through January 1, 2024, plus interest at a rate reset periodically of 275 basis points over selected LIBOR maturity (which was 5.15% at December 31, 2018).	18,218	19,226
Secured loan payable of \$4,116, payable in monthly installments of \$49 through January 1, 2024, plus interest at a rate reset periodically of 325 basis points over selected LIBOR maturity (which was 5.65% at December 31, 2018).	2,989	3,577
Total borrowings	<u>29,114</u>	<u>32,350</u>
Less: unamortized debt issuance costs	231	277
	<u>\$ 28,883</u>	<u>\$ 32,073</u>

Aggregate maturities of the Company's borrowings as of December 31, 2018 are summarized as follows:

Year ending December 31	
2019	\$ 3,236
2020	3,236
2021	3,236
2022	3,236
2023	2,942
Thereafter	<u>13,228</u>
	<u>\$ 29,114</u>

On December 28, 2016, TSM entered into a \$35,500 credit agreement with a commercial bank in Puerto Rico. The agreement consists of three term loans: (i) Term Loan A in the principal amount of \$11,187, (ii) Term Loan B in the principal amount of \$20,150 and (iii) Term Loan C in the principal amount of \$4,116. Term Loan A matures in October 2023 while the Term Loans B and C mature in January 2024. Term Loan A was used to refinance a previous \$41,000 secured loan payable with the same commercial bank. Proceeds from Term Loans B and C were received on January 11, 2017 and were used to prepay the outstanding principal amount plus accrued interest of the 6.6% Senior Unsecured Notes due December 2020 (\$24,000) and fund a portion of a debt service reserve for the loan (approximately \$200). Interest payable commenced on January 1, 2017, in the case of Term Loan A, and on February 1, 2017, in the case of Term Loan B and Term Loan

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C. The Credit Agreement includes certain financial and non-financial covenants, including negative covenants imposing certain restrictions on the Corporation's business. The Company was in compliance with all these covenants as of December 31, 2018.

This credit agreement is guaranteed by a first mortgage held by the bank on the Company's land, building, and substantially all leasehold improvements, as collateral for the term of the loan under a continuing general security agreement.

The Company may, at its option, upon notice, as specified in the credit agreement, redeem and prepay prior to maturity, all or any part of the loan and from time to time upon the payment of a penalty fee of 3% during the first year, 2% during the second year and 1% during the third year, and thereafter, at par, as specified in the credit agreement, together with accrued and unpaid interest, if any, to the date of redemption specified by the Company.

Interest expense on the above borrowings amounted to \$1,375, \$1,196, and \$1,763, for the years ended December 31, 2018, 2017, and 2016, respectively.

On April 18, 2017, TSA entered into a \$10,000 revolving loan agreement with a commercial bank in Puerto Rico. This line of credit has an interest rate of 30-day LIBOR plus 25 basis points and contains certain financial and non-financial covenants that are customary for this type of facility. This line of credit had an original maturity date of April 17, 2018 and was renewed for an additional year, maturing on April 30, 2019.

14. Reinsurance Activity

The effect of reinsurance on premiums earned and claims incurred is as follows:

	Premiums Earned			Claims Incurred ⁽¹⁾		
	2018	2017	2016	2018	2017	2016
Gross	\$ 3,009,830	\$ 2,893,765	\$ 2,945,017	\$ 2,657,639	\$ 3,010,728	\$ 2,454,758
Ceded	(73,591)	(71,295)	(59,032)	(163,898)	(687,520)	(15,008)
Assumed	2,352	4,462	4,656	3,089	4,099	3,689
Net	<u>\$ 2,938,591</u>	<u>\$ 2,826,932</u>	<u>\$ 2,890,641</u>	<u>\$ 2,496,830</u>	<u>\$ 2,327,307</u>	<u>\$ 2,443,439</u>

(1) The claims incurred disclosed in this table exclude the portion of the change in the liability for future policy benefits amounting to \$30,783, \$25,794, and \$28,752 that is included within the consolidated claims incurred during the years ended December 31, 2018, 2017 and 2016, respectively.

TSS, TSA, TSP and TSV, in accordance with general industry practices, annually purchase reinsurance to protect them from the impact of large unforeseen losses and prevent sudden and unpredictable changes in net income and stockholders' equity of the Company. Reinsurance contracts do not relieve any of the subsidiaries from their obligations to policyholders. In the event that all or any of the reinsuring companies might be unable to meet their obligations under existing reinsurance agreements, the subsidiaries would be liable for such defaulted amounts. During 2018, 2017, and 2016 TSP placed 16.45%, 14.88%, and 13.16% of its reinsurance business with one reinsurance company.

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TSS has excess of loss reinsurance treaties whereby it cedes a portion of its premiums to third parties. Reinsurance contracts are primarily for periods of one year and are subject to modifications and negotiations at each renewal date. Premiums ceded under these contracts amounted to \$1,524, \$2,168, and \$3,148 in 2018, 2017 and 2016, respectively. Claims ceded amounted to \$320, \$463, and \$1,700, in 2018, 2017 and 2016, respectively. Principal reinsurance agreements include an organ transplant excess of loss treaty, which covers:

- For group policies, 80% of the claims up to a maximum of \$800 (80% of \$1,000), per person, per life. For other group policies with other options, the agreement covers 80% of the claims up to a maximum of \$400 (80% of \$500), per person, per life, or 80% of the claims up to a maximum of \$200 (80% of \$250), per person, per life.
- For policies provided to the active and retired employees of the Commonwealth of Puerto Rico and its instrumentalities, the treaty covers 100% of the claims up to a maximum of \$1,000 per person, per life with major medical coverage, only if the covered person uses providers that are members of TSS network.
- For policies provided to the municipalities of Puerto Rico, the treaty covers 100% of the claims up to a maximum of \$250, per person, per life, with plans with lifetime limits and all other plans 100% of the claims up to a maximum of \$1,000, per person, per life.

TSA has an excess of loss reinsurance treaty whereby it cedes a portion of its premiums to a third party. This reinsurance contract is for a period of one year and is subject to modifications and negotiations in each renewal date. Premiums ceded under this contract amounted to \$2,300 and \$1,224, in 2018 and 2017, respectively. Claims ceded amounted to \$1,804 and \$1,360, in 2018 and 2017, respectively. This reinsurance agreement includes an excess of loss reinsurance coverage for certain hospital inpatient, hospital outpatient, ambulance, and physician services as well as pharmaceutical drugs. This agreement covers a maximum of \$2,000 per person, per agreement term.

TSP utilized facultative reinsurance, pro rata, and excess of loss reinsurance treaties to manage its exposure to losses, including those from catastrophe events. TSP has geographic exposure to catastrophe losses from hurricanes and earthquakes. The incidence and severity of catastrophes are inherently unpredictable. Under these treaties, TSP ceded premiums written were \$60,354, \$62,268, and \$45,957, in 2018, 2017, and 2016, respectively. In 2018 and 2017, TSP ceded claims incurred amounting to \$152,704 and \$678,624, respectively, related to losses caused by Hurricanes Irma and Maria.

During 2018, as part of the catastrophe program, TSP signed a multiyear reinsurance contract providing for retroactive and prospective reinsurance coverage. The retroactive coverage resulted in a deferred gain on retroactive reinsurance of \$25,000 as of December 31, 2018, which is presented within the accounts payable and accruals in the accompanying consolidated balance sheets. The deferred gain on the retroactive reinsurance will be amortized using the recovery method. The recovery method provides for the amortization in proportion to the estimated recoveries made as of the reporting date as a percentage of total estimated recoveries.

Ceded unearned reinsurance premiums arising from TSP reinsurance transactions amounted to \$11,760 and \$12,393 as of December 31, 2018 and 2017, respectively, and are reported as other assets in the accompanying consolidated balance sheets.

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Most principal reinsurance contracts are for a period of one year and are subject to modifications and negotiations in each renewal. Current property and catastrophe reinsurance program was renewed effective April 1, 2018 for the twelve-month period ending March 31, 2019. Other contracts were renewed as expiring on January 1, 2019.

Principal reinsurance agreements are as follows:

- Casualty excess of loss treaty provides reinsurance for losses up to \$12,000, subject to a retention of \$225.
- Medical malpractice excess of loss treaty provides reinsurance for losses up to \$3,000, subject to a retention of \$150.
- Property reinsurance treaty includes proportional cessions and a per risk excess of loss contract limiting losses to \$325 in \$30,000 risks.
- Catastrophe protection is purchased limiting losses to \$10,000 per event with losses up to approximately \$915,000.

TSV also cedes insurance with various reinsurance companies under a number of pro rata, excess of loss and catastrophe treaties. Under these treaties, TSV ceded premiums of \$8,780, \$8,826, and \$8,838, in 2018, 2017, and 2016, respectively. Principal reinsurance agreements are as follows:

- Group life insurance facultative agreement, reinsuring risk in excess of \$25 of certain group life policies and a combined pro rata and excess of loss agreement effective July 1, 2008, reinsuring 50% of the risk up to \$200 and ceding the excess.
- Facultative pro rata agreements for the long-term disability insurance, reinsuring 65% of the risk.
- Several reinsurance agreements, mostly on an excess of loss basis up to a maximum retention of \$200.
- Excess of loss agreement for the major medical business in Costa Rica reinsuring 100% of all claims over \$35.

TSV participates in various retrocession reinsurance agreements. The retrocessions are based on group life and health reinsurance business pools for which TSV has participations ranging from 6.7% to 10% of the total reinsurance facility. TSV share of the reinsurer's gross liability is limited to a maximum that ranges depending on the agreement from \$50 to \$500 per covered life. The agreements cover new and renewal business for a period of twelve months and may be cancelled subject to ninety days written notice at any anniversary date.

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15. Income Taxes

The Company and its subsidiaries are subject to Puerto Rico income taxes. Under Puerto Rico income tax law, the Company is not allowed to file consolidated tax returns with its subsidiaries. The Company's insurance subsidiaries are also subject to U.S. federal income taxes for foreign source dividend income. The Company is potentially subject to income tax audits in the Commonwealth of Puerto Rico for the taxable year 2015 and after, until the applicable statute of limitations expires. Tax audits by their nature are often complex and can require several years to complete.

Managed Care and Property and Casualty corporations are taxed essentially the same as other corporations, with taxable income primarily determined on the basis of the statutory annual statements filed with the insurance regulatory authorities. The corporations are also subject to an alternative minimum income tax, which is calculated based on the formula established by existing tax laws. Any alternative minimum income tax paid may be used as a credit against the excess, if any, of regular income tax over the alternative minimum income tax in future years up to a limit of 25% of the excess.

The Company, through one of its Managed Care corporations, has a branch in the USVI that is subject to a 5% premium tax on policies underwritten therein. As a qualified foreign insurance company, the Company is subject to income taxes in the USVI, which has implemented a mirror tax law based on the U.S. Internal Revenue Code. The branch operations in the USVI had certain net operating losses for USVI tax purposes for which a valuation allowance has been recorded.

Companies within our Life Insurance segment operate as qualified domestic life insurance companies and are subject to the alternative minimum tax and taxes on its capital gains.

On December 22, 2017, U.S Government enacted PL 115-97, better known as the Tax Cut and Jobs Act (TCJA). The TCJA incorporates a series of changes in tax rates at the federal level applicable for taxable years beginning after December 31, 2017 and before January 1, 2026. The U.S. federal maximum corporate income tax rate is reduced from 35% to a 21% flat rate, this change did not have a significant impact for the Company and its insurance subsidiaries are only taxed in that jurisdiction for passive income earned on investments, which continue to be subject to withholding at source at its gross level. In addition, the TCJA incorporates restrictions on insurance business exception to passive foreign investment company (PFIC) rules, that were taxed under the PFIC's earnings, subject to an exception for certain income derived in the active conduct of an insurance business. At the moment, no significant impact for the Company has been identified. We annually test our compliance with the new guidelines for Section 1297 PFIC test, at the insurance subsidiary level.

On December 10, 2018, the Puerto Rico Government signed in to Law by, P C 1544, better known as the Puerto Rico Tax Reform, now Act 257 of 2018. With this Law, additional amendments are incorporated to the Puerto Rico Internal Revenue Code. Approved changes include: (i) a decrease in the maximum corporate tax rate from 39% to 37.5%; (ii) an increase from 80% to a 90% in the amount of net operating loss carryover deduction available to be claimed against current year net income for regular tax purposes; (iii) an increase in the withholding at source for services rendered from 7% to 10% ; (iv) a limitation in the amounts of net operating losses generated by a corporate shareholder allowed to be netted against net income distributed from a flow-through investment, not permitted for taxable years beginning after December 31, 2018; and (v) a revised large taxpayer definition to include flow-through entities and extend the determination of audited financial statement requirements at the group level. The Puerto Rico Tax Reform also adds requirements for the deductibility of certain expenses as well as disclosure requirements related to any uncertain tax

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position (UTP) recorded following GAAP. All of these changes are effective for taxable years beginning January 1, 2019. During the year ended December 31, 2018, the Company recorded an additional deferred tax expense of \$3,165 million related to the impact that the lower corporate tax rate had in our net deferred tax assets.

Federal income taxes recognized by the Company's insurance subsidiaries amounted to approximately \$1,147, \$985, and \$733, in 2018, 2017, and 2016, respectively.

All other corporations within the group are subject to Puerto Rico income taxes as regular corporations, as defined in the P.R. Internal Revenue Code, as amended.

The components of income tax expense (benefit) consisted of the following:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Current income tax expense	\$ 2,212	\$ 34,412	\$ 1,981
Deferred income tax benefit	(32,078)	(9,916)	(8,326)
Total income tax (benefit) expense	<u>\$ (29,866)</u>	<u>\$ 24,496</u>	<u>\$ (6,345)</u>

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The income tax (benefit) expense differs from the amount computed by applying the Puerto Rico statutory income tax rate to the income before income taxes as a result of the following:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
(Loss) income before taxes	\$ (93,172)	\$ 78,977	\$ 11,086
Statutory tax rate	39.00%	39.00%	39.00%
Income tax (benefit) expense at statutory rate	(36,337)	30,801	4,324
(Decrease) increase in taxes resulting from			
Exempt income, net	(2,330)	(3,853)	(5,158)
Effect of taxing life insurance operations as a qualified domestic life insurance company instead of as a regular corporation	(3,445)	(4,871)	(5,033)
Effect of taxing capital gains at a preferential rate	4,819	(2,116)	(3,799)
Adjustment to deferred tax assets and liabilities for changes in effective tax rates	9,217	(120)	1,669
Other adjustments to deferred tax assets and liabilities	(43)	836	2,852
Effect of extraordinary dividend distribution from the JUA Association - reported net of taxes in other income	-	(922)	(151)
Charges against the catastrophe loss reserve	-	1,567	-
Allowance for doubtful receivables recapture	-	2,688	-
Tax credit benefit	(306)	(555)	(709)
Tax returns to provision true up	(798)	363	(181)
Subtotal	<u>7,114</u>	<u>(6,983)</u>	<u>(10,510)</u>
Other permanent disallowances, net:			
Disallowance of expenses related to exempt interest income	-	-	58
Disallowed interest expense	-	-	8
Other	(229)	50	-
Total other permanent differences	<u>(229)</u>	<u>50</u>	<u>66</u>
Other adjustments	(414)	628	(225)
Total income tax (benefit) expense	<u>\$ (29,866)</u>	<u>\$ 24,496</u>	<u>\$ (6,345)</u>

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Deferred income taxes reflect the tax effects of temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and income tax purposes. The net deferred tax asset at December 31, 2018 and 2017 of the Company and its subsidiaries is composed of the following:

	<u>2018</u>	<u>2017</u>
Deferred tax assets		
Allowance for doubtful receivables	\$ 14,092	\$ 11,787
Liability for pension benefits	12,846	13,826
Postretirement benefits	527	662
Deferred compensation	2,202	2,168
Accumulated depreciation	979	1,296
Impairment loss on investments	765	950
Contingency reserves	75	1,950
Share-based compensation	5,587	6,795
Alternative minimum income tax credit	2,627	1,874
Purchased tax credits	1,229	2,767
Net operating loss	60,731	38,839
Reinsurance agreement	9,375	-
Accrued liabilities	4,292	3,271
Difference in tax basis of investments portfolio	320	-
Other	188	873
	<u>115,835</u>	<u>87,058</u>
Gross deferred tax assets		
Less: valuation allowance	(9,867)	(8,283)
Deferred tax assets	<u>105,968</u>	<u>78,775</u>
Deferred tax liabilities		
Deferred policy acquisition costs	(6,382)	(7,323)
Catastrophe loss reserve	(12,385)	(6,371)
Unrealized gain on securities available for sale	(6,781)	(19,440)
Unrealized gain on equity investments	(2,773)	-
Difference in tax basis of investments portfolio	-	(220)
Unamortized debt issue costs	(87)	(108)
Intangible asset	(909)	(1,546)
Employee benefits plan	(886)	(535)
	<u>(30,203)</u>	<u>(35,543)</u>
Gross deferred tax liabilities		
Net deferred tax asset	<u>\$ 75,765</u>	<u>\$ 43,232</u>

The net deferred tax asset shown in the table above at December 31, 2018 and 2017 is reflected in the consolidated balance sheets as \$79,010 and \$65,123, respectively, in deferred tax assets and \$3,245 and \$21,891, in deferred tax liabilities, respectively, reflecting the aggregate deferred tax assets or liabilities of individual tax-paying subsidiaries of the Company.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization

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of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management believes that it is more likely than not that the Company will realize the benefits of these deductible differences. The valuation allowance is mostly related to the net operating losses generated by the Company's USVI operations and the health clinic's operations based on the available evidence are not considered to be realizable at the reporting dates.

At December 31, 2018, the Company and its subsidiaries have net operating loss carry-forwards for Puerto Rico income tax purposes of approximately \$176,977, which are available to offset future taxable income for up to December 2027. The carryforwards generally expire in 2026 through 2027. Except for the valuation allowance described in the previous paragraph, the Company concluded that as of December 31, 2018, it is more likely than not that the entities that have these net operating loss carry-forwards will generate sufficient taxable income within the applicable net operating loss carry-forward periods to realize its deferred tax asset. This conclusion is based on the historical results of each entity, adjusted to exclude non-recurring conditions, and the forecast of future profitability. Management will continue to evaluate, on a quarterly basis, if there are any significant events that will affect the Company's ability to utilize these deferred tax assets.

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16. Pension Plans

Non-contributory Defined-Benefit Pension Plan

The Company sponsors a non-contributory defined-benefit pension plan for its employees and for the employees of certain subsidiaries. Pension benefits begin to vest after five years of vesting service, as defined, and are based on years of service and final average salary, as defined. The funding policy is to contribute to the plan as necessary to meet the minimum funding requirements set forth in the Employee Retirement Income Security Act of 1974, as amended, plus such additional amounts as the Company may determine to be appropriate from time to time. The measurement date used to determine pension benefit for the pension plan is December 31.

In December 2016, the Company announced that effective January 31, 2017, it would freeze the pay and service amounts used to calculate pension benefits for active employees who participated in the pension plan. Therefore, as of the effective date, active employees in the pension plan do not accrue additional benefits for future service and eligible compensation received.

The following table sets forth the plan's benefit obligations, fair value of plan assets, and funded status as of December 31, 2018 and 2017, accordingly:

	<u>2018</u>	<u>2017</u>
Change in benefit obligation		
Benefit obligation at beginning of year	\$ 185,052	\$ 163,877
Service cost	-	223
Interest cost	6,853	7,186
Benefit payments	(4,466)	(10,503)
Actuarial (gain) loss	(18,114)	24,269
Settlements	(9,848)	-
Benefit obligation at end of year	<u>\$ 159,477</u>	<u>\$ 185,052</u>
Accumulated benefit obligation at end of year	\$ 159,477	\$ 185,052
Change in fair value of plan assets		
Fair value of plan assets at beginning of year	\$ 158,879	\$ 140,398
Actual return on assets	(11,608)	24,984
Employer contributions	2,000	4,000
Settlements	(9,848)	-
Benefit payments	(4,466)	(10,503)
Fair value of plan assets at end of year	<u>\$ 134,957</u>	<u>\$ 158,879</u>
Funded status at end of year	\$ (24,520)	\$ (26,173)

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The amounts recognized in the consolidated balance sheets as of December 31, 2018 and 2017 consist of the following:

	<u>2018</u>	<u>2017</u>
Pension liability	\$ 24,520	\$ 26,173
Net actuarial loss recognized in accumulated other comprehensive loss, net of a deferred tax of \$10,469 and \$10,176 in 2018 and 2017, respectively	23,691	24,540

The following assumptions were used on a weighted average basis to determine benefits obligations of the plan as of December 31, 2018 and 2017.

	<u>2018</u>	<u>2017</u>
Discount rate	4.50%	3.75%
Expected return on plan assets	6.50%	6.50%
Rate of compensation increase	N/A	N/A

The components of net periodic benefit cost and other amounts recognized in other comprehensive income for 2018, 2017, and 2016 were as follows:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Components of net periodic benefit cost			
Service cost	\$ -	\$ 223	\$ 3,640
Interest cost	6,853	7,186	8,749
Expected return on plan assets	(9,020)	(8,740)	(9,003)
Prior service benefit	-	-	(450)
Actuarial loss	961	369	4,028
Settlement loss	2,110	-	-
Net periodic benefit cost	<u>\$ 904</u>	<u>\$ (962)</u>	<u>\$ 6,964</u>

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Other changes in plan assets and benefit obligations recognized in other comprehensive income			
Net actuarial (gain) loss	\$ 2,515	\$ 8,024	\$ (24,628)
Amortization of:			
Prior service credit	-	-	2,225
Actuarial loss	(3,071)	(369)	(4,028)
Total recognized in other comprehensive income	<u>\$ (556)</u>	<u>\$ 7,655</u>	<u>\$ (26,431)</u>

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Net periodic benefit cost includes settlement charges as a result of retirees selecting lump-sum distributions. Settlement charges may increase in the future if the number of eligible participants deciding to receive distributions and the amount of their benefits increases.

The Company recognized a pre-tax curtailment income of \$1,773 during the year ended December 31, 2016 resulting from the freezing of the plan that was effective January 31, 2017.

The estimated net actuarial loss that will be amortized from accumulated other comprehensive loss into net periodic pension benefits cost during the next twelve months is \$358.

The following assumptions were used on a weighted average basis in computing the periodic benefit cost for the years ended December 31, 2018, 2017, and 2016:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Discount rate	3.75%	4.50%	4.75%
Expected return on plan assets	6.50%	6.50%	7.00%
Rate of compensation increase	N/A	N/A	Graded; 3.50% to 8.00%

The basis of the overall expected long-term rate of return on assets assumption is a forward-looking approach based on the current long-term capital market outlook assumptions of the assets categories in which the trust invests and the trust's target asset allocation. At December 31, 2018, the assumed target asset allocation for the program is: 45% to 55% in equity securities, 36% to 44% in debt securities, and 6% to 14% in other securities. Using a mean-variance model to project returns over a 30-year horizon under the target asset allocation, the 35 to 65 percentile range of annual rates of return is 5.8% to 7.2%. The Company selected a rate from within this range of 6.50% for 2018 and 6.50% for 2017, which reflects the Company's best estimate for this assumption based on the data described above, information on the historical returns on assets invested in the pension trust, and expected future conditions. This rate is net of both investment related expenses and a 0.15% reduction for other administrative expenses charged to the trust.

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Plan Assets

Plan assets recorded at fair value are categorized based upon the level of judgment associated with the inputs used to measure their fair value. For level inputs and input definition, see note 10.

The following table summarizes fair value measurements by level at December 31, 2018 and 2017 for assets measured at fair value on a recurring basis:

	2018				
	Level 1	Level 2	Level 3	Total	NAV
Government obligations	\$ -	\$ 6,856	\$ -	\$ 6,856	\$ -
Non-agency backed securities	-	759	-	759	-
Corporate obligations	-	10,490	-	10,490	-
Limited Liability Corporations	-	-	-	-	97,660
Real estate	-	-	-	-	7,975
Registered investments	2,328	1,610	-	3,938	-
Common/Collective trusts	-	4,231	-	4,231	1,898
Common stocks	1,566	-	-	1,566	-
Preferred stocks	6	23	-	29	-
Forward foreign currency contracts	-	42	-	42	-
Interest-bearing cash	700	-	-	700	-
Derivatives	-	44	-	44	-
	\$ 4,600	\$ 24,055	\$ -	\$ 28,655	\$ 107,533

	2017				
	Level 1	Level 2	Level 3	Total	NAV
Government obligations	\$ -	\$ 7,131	\$ -	\$ 7,131	\$ -
Non-agency backed securities	-	641	-	641	-
Corporate obligations	-	8,560	-	8,560	-
Limited Liability Corporations	-	-	-	-	119,581
Real estate	-	-	-	-	7,568
Registered investments	3,388	659	-	4,047	-
Hedge funds	-	8,808	-	8,808	1,972
Common stocks	1,920	-	-	1,920	-
Preferred stocks	23	17	-	40	-
Interest-bearing cash	501	-	-	501	-
Derivatives	(1)	17	-	16	-
	\$ 5,831	\$ 25,833	\$ -	\$ 31,664	\$ 129,121

The Company's plan assets are invested in the National Retirement Trust. The National Retirement Trust was formed to provide financial and legal resources to help members of the BCBSA offer retirement benefits to their employees.

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The investment program for the National Retirement Trust is based on the precepts of capital market theory that are generally accepted and followed by institutional investors, who by definition are long-term oriented investors. This philosophy holds that:

- Increasing risk is rewarded with compensating returns over time, and therefore, prudent risk taking is justifiable for long-term investors.
- Risk can be controlled through diversification of asset classes and investment approaches, as well as diversification of individual securities.
- Risk is reduced by time, and over time the relative performance of different asset classes is reasonably consistent. Over the long-term, equity investments have provided and should continue to provide superior returns over other security types. Fixed-income securities can dampen volatility and provide liquidity in periods of depressed economic activity. Lengthening duration of fixed income securities may reduce surplus volatility.
- The strategic or long-term allocation of assets among various asset classes is an important driver of long-term returns.
- Relative performance of various asset classes is unpredictable in the short-term and attempts to shift tactically between asset classes are unlikely to be rewarded.

Investments will be made for the sole interest of the participants and beneficiaries of the programs participating in the National Retirement Trust. Accordingly, the assets of the National Retirement Trust shall be invested in accordance with these objectives:

- To ensure assets are available to meet current and future obligations of the participating programs when due.
- To earn the maximum return that can be realistically achieved in the markets over the long-term at a specified and controlled level of risk in order to minimize future contributions.
- To invest assets with consideration of the liability characteristics in order to better align assets and liabilities.
- To invest the assets with the care, skill, and diligence that a prudent person acting in a like capacity would undertake. In the process, the Administration of the Trust has the objective of controlling the costs involved with administering and managing the investments of the National Retirement Trust.

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Cash Flows

The Company expects to contribute \$2,000 to its pension program in 2019.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

Year ending December 31	
2019	\$ 9,572
2020	9,145
2021	9,329
2022	9,214
2023	9,278
2024 – 2028	49,475

Non-contributory Supplemental Pension Plan

In addition, the Company sponsors a non-contributory supplemental pension plan. This plan covers employees with qualified defined benefit retirement plan benefits limited by the U.S. Internal Revenue Code maximum compensation and benefit limits. At December 31, 2018 and 2017, the Company has recorded a pension liability of \$6,754 and \$7,499, respectively. The charge to accumulated other comprehensive loss related to the non-contributory pension plan at December 31, 2018 and 2017 amounted to \$35 and \$445, respectively, net of a deferred tax asset of \$61 and \$290, respectively.

17. Catastrophe Loss Reserve and Trust Fund

In accordance with Chapter 25 of the Puerto Rico Insurance Code, as amended, TSP is required to record a catastrophe loss reserve. This catastrophe loss reserve is supported by a trust fund for the payment of catastrophe losses. The reserve increases by amounts determined by applying a contribution rate, not in excess of 5%, to catastrophe written premiums as instructed annually by the Commissioner of Insurance, unless the level of the reserve exceeds 8% of catastrophe exposure, as defined. The reserve also increases by an amount equal to the resulting return in the supporting trust fund and decreases by payments on catastrophe losses or authorized withdrawals from the trust fund. Additions to the catastrophe loss reserve are deductible for income tax purposes.

This trust may invest its funds in securities authorized by the Insurance Code, but not in investments whose value may be affected by hazards covered by the catastrophic insurance losses. The interest earned on these investments and any realized gains (loss) on investment transactions are part of the trust fund and are recorded as income (expense) of the Company. An amount equal to the investment returns is recorded as an addition to the trust fund.

During the year ended December 31, 2018, TSP received the approval of the Commissioner of Insurance and withdrew \$10,000 from the catastrophe fund following the payment for catastrophe losses related to the impact of Hurricanes Irma and Maria in September 2017.

The interest earning assets in this fund, which amounted to \$38,978 and \$48,363 as of December 31, 2018 and 2017, respectively, are to be used solely and exclusively to pay catastrophe losses covered under policies written in Puerto Rico.

TSP is required to contribute to the trust fund, if needed or necessary, on or before January 31 of the following year. Contributions are determined by a rate determined or established by the Commissioner of Insurance for the catastrophe policies written in that year. No contribution was

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required for 2018 and 2017 since the level of the catastrophe reserve exceeds 8% of the catastrophe exposure.

The amount in the trust fund may be withdrawn or released in the case that TSP ceases to underwrite risks subject to catastrophe losses. Also, authorized withdrawals are allowed when the catastrophe loss reserve exceeds 8% of the catastrophe exposure, as defined.

TSP retained earnings are restricted in the accompanying consolidated balance sheets by the total catastrophe loss reserve balance, which as of December 31, 2018 and 2017 amounted to \$37,749 and \$46,578, respectively.

18. Stockholders' Equity

a. Common Stock

On November 12, 2015, the Company converted 1,426,721 issued and outstanding Class A shares into Class B common stock purchased pursuant to the provisions of the Articles of incorporation approved by Class A shareholders at the time of the Company's Initial Public Offering.

b. Preferred Stock

Authorized capital stock includes 100,000,000 of preferred stock with a par value of \$1.00 per share. As of December 31, 2018 and 2017, there are no issued and outstanding preferred shares.

c. Liquidity Requirements

As members of the BCBSA, the Company, TSS, and TSA are required by membership standards of this association to maintain liquidity as defined by BCBSA. That is, to maintain total adjusted capital at or above 375% of Health Risk-Based Capital (HRBC) Authorized Control Level (ACL) as defined by the National Association of Insurance Commissioners (NAIC) for the for Primary Licensee (TSM) and Larger BCBS Controlled Affiliate (TSS) and 100% HRBC ACL for the Smaller BCBS Controlled Affiliate (TSA).

d. Dividends

As a holding company, the Company's most significant assets are the common shares of its subsidiaries. The principal sources of funds available to the Company are rental income and dividends from its subsidiaries, which are used to fund our debt service and operating expenses.

The Company is subject to the provisions of the General Corporation Law of Puerto Rico, which restricts the declaration and payment of dividends by corporations organized pursuant to the laws of Puerto Rico. These provisions provide that Puerto Rico corporations may only declare dividends charged to their retained earnings or, in the absence of retained earnings, net profits of the fiscal year in which the dividend is declared and/or the preceding fiscal year.

The Company's ability to pay dividends is dependent, among other factors, on its ability to collect cash dividends from its subsidiaries, which are subject to regulatory requirements, which may

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restrict their ability to declare and pay dividends or distributions. In addition, an outstanding secured term loan restricts our ability to pay dividends in the event of default (see note 13).

The accumulated earnings of TSS, TSA, TSV, TSB and TSP are restricted as to the payment of dividends by statutory limitations applicable to domestic insurance companies. Under Puerto Rico insurance regulations, the regulated subsidiaries are permitted, without requesting prior regulatory approval, to pay dividends as long as the aggregate amount of all such dividends in any calendar year does not exceed the lesser of: (i) 10% of its surplus as of the end of the immediately preceding calendar year; or (ii) its statutory net gain from operations for the immediately preceding calendar year (excluding realized capital gains). Regulated subsidiaries will be permitted to pay dividends in excess of the lesser of such two amounts only if notice of its intent to declare such a dividend and the amount thereof is filed with the Commissioner of Insurance and such dividend is not disapproved within 30 days of its filing. As of December 31, 2018, the dividends permitted to be distributed in 2019 by the regulated subsidiaries without prior regulatory approval from the Commissioner of Insurance amounted to approximately \$26,000.

19. Stock Repurchase Programs

The Company repurchases shares through open market transactions, in accordance with Rule 10b-18 of the Securities Exchange Act of 1934, as amended, under repurchase programs authorized by the Board of Directors. Shares purchased under share repurchase programs are retired and returned to authorized and unissued status.

A summary of share repurchase programs in place during the three-year-period ended December 31, 2018 is as follows:

- In November 2015 the Company's Board of Directors authorized a \$25,000 repurchase program (2015 \$25,000 program) of its Class B common stock. This program was completed on September 14, 2016.
- In August 2017 the Company's Board of Directors authorized a \$30,000 repurchase program (2017 \$30,000 program) of its Class B common stock. In February 2018 the Company's Board of Directors authorized a \$25,000 expansion of this program.

The stock repurchase activity under stock repurchase programs for the years ended December 31 is summarized as follows:

	2018			2017			2016		
	Shares Repurchased	Average Share Price	Amount Repurchased	Shares Repurchased	Average Share Price	Amount Repurchased	Shares Repurchased	Average Share Price	Amount Repurchased
2017 \$30,000 program	903,888	\$ 24.76	\$ 22,390	861,415	\$ 23.38	\$ 20,220	-	\$ -	\$ -
2015 \$25,000 program	-	-	-	-	-	-	951,831	22.54	21,370
Total	903,888	\$ 24.76	\$ 22,390	861,415	\$ 23.38	\$ 20,220	951,831	\$ 22.54	\$ 21,370

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20. Comprehensive Income

The accumulated balances for each classification of other comprehensive income are as follows:

	Unrealized Gains on Securities	Liability for Pension Benefits	Accumulated Other Comprehensive Income
Beginning balance at December 31, 2017	\$ 76,238	\$ (24,984)	\$ 51,254
Cumulative effect adjustment due to implementation of ASU 2016-01	(39,882)	-	(39,882)
Net current period change	(19,500)	1,360	(18,140)
Reclassification adjustments for gains and losses reclassified in income	10,452	(622)	9,830
Ending balance at December 31, 2018	\$ 27,308	\$ (24,246)	\$ 3,062

The related deferred tax effects allocated to each component of other comprehensive income in the accompanying consolidated statements of stockholders' equity and comprehensive income in 2018, 2017 and 2016 are as follows:

	2018		
	Before-Tax Amount	Deferred Tax (Expense) Benefit	Net-of-Tax Amount
Unrealized holding gains on securities arising during the period	\$ (24,375)	\$ 4,875	\$ (19,500)
Less reclassification adjustment for gains and losses realized in income	13,457	(3,005)	10,452
Net change in unrealized gain	(10,918)	1,870	(9,048)
Liability for pension benefits:			
Reclassification adjustment for amortization of net losses from past experience and prior service costs	(995)	373	(622)
Net change arising from assumptions and plan changes and experience	2,190	(830)	1,360
Net change in liability for pension benefits	1,195	(457)	738
Net current period change	\$ (9,723)	\$ 1,413	\$ (8,310)

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	2017		
	Before-Tax Amount	Deferred Tax (Expense) Benefit	Net-of-Tax Amount
Unrealized holding gains on securities arising during the period	\$ 28,544	\$ (5,708)	\$ 22,836
Less reclassification adjustment for gains and losses realized in income	(10,831)	1,862	(8,969)
Net change in unrealized gain	17,713	(3,846)	13,867
Liability for pension benefits:			
Reclassification adjustment for amortization of net losses from past experience and prior service costs	5	(2)	3
Net change arising from assumptions and plan changes and experience	(8,215)	3,204	(5,011)
Net change in liability for pension benefits	(8,210)	3,202	(5,008)
Net current period change	\$ 9,503	\$ (644)	\$ 8,859
	2016		
	Before-Tax Amount	Deferred Tax (Expense) Benefit	Net-of-Tax Amount
Unrealized holding gains on securities arising during the period	\$ 18,357	\$ (3,596)	\$ 14,761
Less reclassification adjustment for gains and losses realized in income	(17,379)	2,511	(14,868)
Net change in unrealized gain	978	(1,085)	(107)
Liability for pension benefits:			
Reclassification adjustment for amortization of net losses from past experience and prior service costs	1,888	(737)	1,151
Net change arising from assumptions and plan changes and experience	25,783	(10,055)	15,728
Net change in liability for pension benefits	27,671	(10,792)	16,879
Net current period change	\$ 28,649	\$ (11,877)	\$ 16,772

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21. Share-Based Compensation

In December 2007, the Company adopted the 2007 Incentive Plan (the 2007 plan), which permits the Board to grant stock options, restricted stock awards and performance awards to eligible officers, directors and employees. The 2007 plan authorized the granting of up to 4,700,000 of Class B common shares of authorized but unissued stock. The 2007 plan was terminated in April 2017, when the 2017 Incentive Plan (the 2017 plan) was adopted. The 2017 plan permits the Board to grant stock options, stock appreciation rights (SARs), restricted stock, restricted stock units, performance awards, and other stock-based awards, to our officers and employees. In addition, the 2017 plan authorizes the grant of equity-based compensation incentives to our directors and to any independent contractor and consultants. The 2017 plan authorizes the granting of up to 1,700,000 of Class B common shares plus the number of shares that were subject to any outstanding awards under the 2007 plan that are forfeited, cancelled, expire, terminate or otherwise lapse, in whole or in part, without the delivery of the shares. At December 31, 2018, there were 1,286,373 shares available for the Company to grant under the 2017 Plan.

Stock options and SARs can be granted with an exercise price, which shall not be less than the stock's fair market value at the grant date. The term of each stock options and SARs shall be fixed by the Board of Directors but shall not exceed 10 years from the date of grant. The restricted stock, restricted stock units, and performance awards are issued at the fair value of the stock on the grant date. Restricted stock awards and restricted stock units vest in installments, as stipulated in each restricted stock agreement. Performance awards vest on the last day of the performance period, provided that at least minimum performance standards are achieved.

There was no stock option activity during the years ended December 31, 2018 and 2017. There were 4,440 exercised options during 2016. No options were granted during the three years ended December 31, 2018, 2017 and 2016. No cash was received from stock options exercises during the years ended December 31, 2018, 2017 and 2016. During the year ended December 31, 2018, 29,779 shares were repurchased and retired as the result of non-cash tax withholding upon vesting of shares. During the year ended December 31, 2016, 2,290 shares were repurchased and retired as a result of non-cash exercise of stock options. No shares were repurchased and retired as a result of non-cash exercise of stock options or non-cash tax withholding upon vesting of shares during year ended December 31, 2017.

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A summary of the status of the Company's non-vested restricted and performance shares as of December 31, 2018, and changes during the year ended December 31, 2018, are presented below:

	Restricted Awards		Performance Awards	
	Number of Shares	Weighted Average Fair Value	Number of Shares	Weighted Average Exercise Price
Outstanding balance at January 1, 2018	217,687	\$ 19.26	536,124	\$ 20.47
Granted	116,316	28.49	249,575	26.50
Lapsed	(126,483)	18.90	16,607	3.62
Forfeited (due to termination)	(1,647)	21.80	(16,384)	20.82
Quantity adjusted (due to performance payout more than 100%), net of forfeited	-	-	(226,084)	22.43
Outstanding balance at December 31, 2018	205,873	\$ 24.67	559,838	\$ 21.86

The weighted average grant date fair value of restricted shares granted during the year 2018, 2017 and 2016 were \$28.49, \$17.78, and \$23.78, respectively. Total fair value of restricted stock vested during the year ended December 31, 2018, 2017 and 2016 was \$2,390, \$1,948 and \$2,335, respectively.

At December 31, 2018, there was \$8,824 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the Plan. That cost is expected to be recognized over a weighted average period of 0.96 years. The Company currently uses authorized and unissued Class B common shares to satisfy share award exercises.

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22. Net Income Available to Stockholders and Basic Net Income per Share

The following table sets forth the computation of basic and diluted earnings per share for the three-year period ended December 31:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Numerator for earnings per share			
Net (loss) income attributable to TSM available to stockholders	\$ (63,302)	\$ 54,486	\$ 17,438
Denominator for basic earnings per share –			
Weighted average of common shares	22,975,385	23,996,503	24,454,435
Effect of dilutive securities	-	71,083	56,658
Denominator for diluted earnings per share	<u>22,975,385</u>	<u>24,067,586</u>	<u>24,511,093</u>
Basic net (loss) income per share attributable to TSM	\$ (2.76)	\$ 2.27	\$ 0.71
Diluted net (loss) income per share attributable to TSM	\$ (2.76)	\$ 2.26	\$ 0.71

The Company excluded the effect of dilutive securities during the year ended December 31, 2018 because their effect would have been anti-dilutive given the net loss attributable to stockholders during this year. If the Company had generated income from continuing operations during the year ended December 31, 2018 the effect of the restricted stock awards on the diluted shares calculation would have been an increase in shares of 81,023 shares.

23. Commitments

The Company leases its regional offices, certain equipment, and warehouse facilities under non-cancelable operating leases. Minimum annual rental commitments at December 31, 2018 under existing agreements are summarized as follows:

Year ending December 31	
2019	\$ 5,214
2020	2,972
2021	1,713
2022	1,220
2023	224
Total	<u>\$ 11,343</u>

Rental expense for 2018, 2017, and 2016 was \$8,924, \$7,991, and \$7,613 respectively.

Pursuant to the provisions of the Puerto Rico Insurance Code and Regulations, TSP is a member of the Compulsory Vehicle Liability Insurance Joint Underwriting Association (JUA). As a participant, TSP shares the risk, proportionately with other members, based on a formula established by the Puerto Rico Insurance Code, of the results and financial condition of the JUA, and accordingly, may be subject to assessments to cover obligations of the JUA or may receive refund distributions for good experience. The Company received \$215 in 2018 as an ordinary dividend. No assessments were received in 2017. During the year ended December 31, 2017, the JUA declared a \$70,000 extraordinary dividend to its members, subject to a special tax rate of 50% as allowed by Act No. 26 of April 29, 2017. There were no extraordinary dividends declared by the JUA in 2018 and 2016.

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The Company receives dividends from the JUA net of applicable tax. During the year ended December 31, 2017, TSP recorded a special distribution of \$2,363, net of tax, which is included as other income in the accompanying consolidated statements of earnings.

24. Contingencies

The Company's business is subject to numerous laws and regulations promulgated by Federal, Puerto Rico, USVI, Costa Rica, BVI, and Anguilla governmental authorities. Compliance with these laws and regulations can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. The Commissioner of Insurance of Puerto Rico, as well as other Federal, Puerto Rico, USVI, Costa Rica, BVI, and Anguilla government authorities, regularly make inquiries and conduct audits concerning the Company's compliance with such laws and regulations. Penalties associated with violations of these laws and regulations may include significant fines and exclusion from participating in certain publicly funded programs and may require the Company to comply with corrective action plans or changes in our practices.

As of December 31, 2018, the Company is involved in various legal actions arising in the ordinary course of business. The Company is also defendant in various other litigations and proceedings, some of which are described below. Where the Company believes that a loss is both probable and estimable, such amounts have been recorded. Although the Company believes the estimates of such losses are reasonable, these estimates could change as a result of further developments in these matters. In other cases, it is at least reasonably possible that the Company may incur a loss related to one or more of the mentioned pending lawsuits or investigations, but the Company is unable to estimate the range of possible loss which may be ultimately realized, either individually or in the aggregate, upon their resolution. The outcome of legal proceedings is inherently uncertain and pending matters for which accruals have not been established have not progressed sufficiently to enable us to estimate a range of possible loss, if any. Given the inherent unpredictability of these matters, it is possible that an adverse outcome in one or more of these matters could have a material effect on the consolidated financial condition, operating results and/or cash flows of the Company.

Additionally, we may face various potential litigation claims that have not been asserted to date, including claims from persons purporting to have rights to acquire shares of the Company on favorable terms pursuant to agreements previously entered by our predecessor managed care subsidiary, Seguros de Servicios de Salud de Puerto Rico, Inc. (SSS), with physicians or dentists who joined our provider network to sell such new provider shares of SSS at a future date (Share Acquisition Agreements) or to have inherited such shares notwithstanding applicable transfer and ownership restrictions.

Claims by Heirs of Former Shareholders

The Company and TSS are defending six individual lawsuits: Vera Sanchez, et al, v. Triple-S; Olivella Zalduondo, et al, v. Seguros de Servicios de Salud, et al; Montilla Lopez, et al v. Seguros de Servicio de Salud, et al; Cebollero Santamaria v. Triple-S Salud, Inc., et al; Ruiz de Porras, et al, v. Triple-S Salud, Inc.; and Irizarry Antonmattei, et al, v. Seguros de Servicio de Salud, et al. All claims were filed in the Puerto Rico Court of First Instance by persons who claim to have inherited a total of 83 shares of the Company of one of its predecessors or affiliates (before giving effect to the 3,000-for-one stock Split). While each case presents unique facts and allegations, the lawsuits generally allege that the redemption of the shares by the Company pursuant to transfer and ownership restrictions contained in the Company's (or its predecessors' or affiliates') articles of incorporation and bylaws was improper. Consequently, the remedy requested by the plaintiffs to be recognized as shareholders of the Company in the corresponding proportion.

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As a result of the Puerto Rico Supreme Court's decision to deny the applicability of the statute of limitations contained in the local securities law, these claims are being litigated on their merits.

On January 11, 2019, local Court of Appeals confirmed Court of First Instance's partial summary judgement in Wanda Irizarry Antonmattei, et al., v. Seguros de Servicios de Salud de Puerto Rico, Inc., et al. ordering the Company to issue 63,000 stock shares in favor of Plaintiffs. The Company filed an appeal before the Supreme Court on February 8, 2019.

In Montilla López, et al. v. Seguros de Servicios de Salud, et al. local Court of First Instance entered summary judgment in favor of Company dismissing all claims on November 2, 2018. Plaintiffs filed an Appeal before Puerto Rico Court of Appeals which the Company opposed on January 18, 2019.

Joint Underwriting Association Litigation

On August 19, 2011, plaintiffs, purportedly a class of motor vehicle owners, filed an action in the United States District Court for the District of Puerto Rico against the JUA and TSP, alleging violations under the Puerto Rico Insurance Code, the Puerto Rico Civil Code, the Racketeer Influenced and Corrupt Organizations Act (RICO) and the local statute against organized crime and money laundering. JUA is a private association created by law to administer a compulsory public liability insurance program for motor vehicles in Puerto Rico (CLI). As required by its enabling act, JUA is composed of all the insurers that underwrite private motor vehicle insurance in Puerto Rico and exceed the minimum underwriting percentage established in such act. TSP is a member of JUA.

In this lawsuit, entitled Noemí Torres Ronda, et al v. JUA et al., plaintiffs allege that the defendants illegally charged and misappropriated a portion of the CLI premiums paid by motor vehicle owners in violation of the Puerto Rico Insurance Code. Specifically, they claim that because the defendants did not incur in acquisition or administration costs allegedly totaling 12% of the premium dollar, charging for such costs constitutes the illegal traffic of premiums. Plaintiffs also claim that the defendants, as members of JUA, violated RICO through various inappropriate actions designed to defraud motor vehicle owners located in Puerto Rico and embezzle a portion of the CLI premiums for their benefit.

Plaintiffs seek the reimbursement of funds for the class amounting to \$406,600 treble damages under RICO, and equitable relief, including a permanent injunction and declaratory judgment barring defendants from their alleged conduct and practices, along with costs and attorneys' fees. Discovery has been completed.

Since 2011, TSP has been defending this claim and, jointly with other defendants, has filed several pleas in connection with the certification of the class and the dismissal of the claim. On April 22, 2016, plaintiff and the three negotiating defendants filed a stipulation of settlement and release which is subject to approval of the court. TSP and the non-settling defendants have objected the filed settlement. On June 18, 2018, defendants moved summary judgment on grounds of res judicata and/or collateral estoppel arising from a parallel dismissal with prejudice confirmed by the Puerto Rico Court of Appeals.

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In re Blue Cross Blue Shield Antitrust Litigation

TSS is a co-defendant with multiple Blue Plans and the Blue Cross Blue Shield Association (BCBSA) in a multi-district class action litigation filed by a group of providers and subscribers on July 24, 2012 and October 1, 2012, respectively, that has since been consolidated by the United States District Court for the Northern District of Alabama, Southern Division, in the case captioned In re Blue Cross Blue Shield Association Antitrust Litigation. Essentially, provider plaintiffs allege that the exclusive service area requirements of the Primary License Agreements with the Blue Plans constitute an illegal horizontal market allocation under federal antitrust laws. As per provider plaintiffs, the quid pro quo for said “market allocation” is a horizontal price fixing and boycott conspiracy” implemented through the Inter-Plans Program Committee (“IPPC”) and whose benefits are allegedly derived through the BCBSA’s Blue Card/National Accounts Program. Among the remedies sought, provider plaintiffs seek increased compensation rates and operational changes. In turn, subscriber plaintiffs allege that the alleged conspiracy to allocate markets have prevented subscribers from being offered competitive prices and resulted in higher premiums for Blue Plan subscribers. Subscribers seek damages in the form of supra-competitive premiums allegedly charged by the Blue Plans and/or the difference between what subscribers have paid the Blues and the lower competitive premiums that non-competing Blues would have charged. Both actions seek injunctive relief.

Prior to consolidation, motions to dismiss were filed by several plans, including TSS - whose request was ultimately denied by the court without prejudice. On April 6, 2015, plaintiffs filed suit in the United States District Court of Puerto Rico against TSS. Said complaint, nonetheless, is believed not to preclude TSS’ jurisdictional arguments. Since inception, the Company has joined BCBSA and other Blue Plans in vigorously contesting these claims. On April 5, 2018, the United States District Court for the Northern District of Alabama, Southern Division, issued its ruling on the parties’ respective motions for partial summary judgment on the standard of review applicable to plaintiffs’ claims under Section 1 of the Sherman Act and subscriber plaintiffs’ motion for partial summary judgment on the Blue Plan’s single entity defense. After considering the “undisputed” facts (for summary judgment purposes only) and evidence currently on record in the light most favorable to defendants, the court essentially found that: (a) the Exclusive Service Areas constitute horizontal market allocations that are subject to the Per Se standard of review; (b) the National Best Efforts Rule constitutes an “output restriction” subject to the Per Se standard of review; (c) there remain genuine issues of material fact as to whether defendants’ conduct can be shielded by the “single entity” defense; and (d) claims concerning the BlueCard Program and uncoupling rules are due to be analyzed under the Rule of Reason standard.

On April 16, 2018, Defendants moved the Federal District Court for the Northern District of Alabama to certify for immediate interlocutory appeal the court’s April 5, 2018 Standard of Review Ruling. On June 12, 2018, judge agreed to grant Defendant’s motion for certification pursuant to 28 U.S.C. §1292(b). Defendants filed their Notice of Appeal on July 12, 2018. On December 12, 2018, the Court of Appeals for the Eleventh Circuit denied Defendants’ petition to appeal the District Court’s Standard of Review Ruling. Given the Court of Appeal’s ruling, Defendants will continue to aggressively defend the case. On January 15, 2019, the parties appeared for a status conference to discuss the litigation’s schedule moving forward and next steps.

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Claims Relating to the Provision of Health Care Services

TSS is a defendant in several claims for collection of monies in connection with the provision of health care services.

On April 17, 2015, ASES notified the Company of a complaint from a medical service provider demanding payment amounting to \$5,073. Claimant alleges that TSS did not pay the claims, paid them incorrectly, or recovered payments from the provider for which TSS did not have the right. TSS answered the complaint and counterclaimed. TSS denies any wrongdoing and will continue to defend this matter vigorously.

On January 12, 2015, American Clinical Solutions LLC, a limited liability company that provides clinical laboratory services filed a complaint in Florida state court alleging that TSM and TSS failed to pay certain clinical laboratory services provided to Blue Cross Blue Shield members. TSS and TSM have filed a motion to dismiss alleging lack of jurisdiction. TSM and TSS also requested a transfer of the case to Puerto Rico. Plaintiff has requested jurisdictional discovery, which is ongoing. The claim amounts to \$5,000. TSS and TSM will continue to vigorously oppose this claim.

25. Statutory Accounting

TSS, TSA, TSV, TSP and TSB (collectively known as the regulated subsidiaries) are regulated by the Commissioner of Insurance. The regulated subsidiaries are required to prepare financial statements using accounting practices prescribed or permitted by the Commissioner of Insurance, which uses a comprehensive basis of accounting other than GAAP. Specifically, the Commissioner of Insurance has adopted the NAIC's Statutory Accounting Principles (NAIC SAP) as the basis of its statutory accounting practices, as long as they do not contravene the provisions of the Puerto Rico Insurance Code, its regulations and the Circular Letters issued by the Commissioner of Insurance. The Commissioner of Insurance may permit other specific practices that may deviate from prescribed practices and NAIC SAP. Statutory accounting principles that are established by state laws and permitted practices mandated by the Commissioner of Insurance may cause the statutory capital and surplus of the regulated subsidiaries to differ from that calculated under the NAIC SAP.

Prescribed statutory accounting practices in Puerto Rico allow TSP to disregard a deferred tax liability resulting from additions to the catastrophe loss reserve trust fund that would otherwise be required under NAIC SAP. The use of prescribed and permitted accounting practices, both individually and in the aggregate, did not change significantly the combined statutory capital and surplus that would have been reported following NAIC SAP, which as of December 31, 2018 and 2017 is approximately 2.1% and 1.0%, respectively, lower than the combined reported statutory capital and surplus.

The regulated subsidiaries are required by the NAIC and the Commissioner of Insurance to submit risk-based capital (RBC) reports following the NAIC's RBC Model Act and accordingly, are subject to certain regulatory actions if their capital levels do not meet minimum specific RBC requirements. RBC is a method developed by the NAIC to determine the minimum amount of statutory capital appropriate for an insurance company to support its overall business operations in consideration of its size and risk profile. The RBC is calculated by applying capital requirement factors to various assets, premiums and reserve items. The factor is higher for those items with greater underlying risk and lower for less risky items. The adequacy of an organization's actual capital can then be measured by a comparison to its RBC as determined by the formula.

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The RBC Model Act requires increasing degrees of regulatory oversight and intervention as an organization's risk-based capital declines. The level of regulatory oversight ranges from requiring organizations to inform and obtain approval from the domiciliary insurance commissioner of a comprehensive financial plan for increasing its RBC, to mandatory regulatory intervention requiring an insurance company to be placed under regulatory control, in a rehabilitation or liquidation proceeding.

The Commissioner of Insurance adopted in 2009 an RBC policy that requires that the regulated entities maintain statutory reserves at or above the "Company Action Level," in order to avoid regulatory monitoring and intervention. The Company action level is currently set at 200% of the RBC for TSA, since it is organized as a health service organization and 300% of the RBC for TSS, TSV, and TSB. The RBC requirement for TSP is 300% but compliance with certain trend analysis can lower this requirement to 200%. As of December 31, 2018, all regulated subsidiaries comply with minimum statutory reserve requirements, except for TSP which is currently in an RBC remediation plan with the Commissioner of Insurance. As of December 31, 2017, all regulated subsidiaries complied with minimum statutory reserve requirements.

The following table sets forth the combined net admitted assets, capital and surplus, RBC requirement, which is our statutory capital and surplus requirement, and net income for the regulated subsidiaries at December 31, 2018, 2017 and 2016:

(dollar amounts in millions)	2018	2017	2016
Net admitted assets	\$ 2,089	\$ 2,102	\$ 1,829
Capital and surplus	602	647	638
RBC requirement	312	301	278
Net (loss) income	(32)	87	24

As more fully described in note 17, a portion of the accumulated earnings and admitted assets of TSP are restricted by the catastrophe loss reserve and the trust fund balance as required by the Insurance Code. The total catastrophe loss reserve and trust fund amounted to \$37,749 and \$38,978 as of December 31, 2018, respectively. The total catastrophe loss reserve and trust fund amounted to \$27,843 and \$48,363 as of December 31, 2017, respectively. In addition, the admitted assets of the regulated subsidiaries are restricted by the investments deposited with the Commissioner of Insurance to comply with requirements of the Insurance Code (see note 3). Investments with an amortized cost of \$1,567 and \$5,229 (fair value of \$1,602 and \$5,571) at December 31, 2018 and 2017, respectively, were deposited with the Commissioner of Insurance. As a result, the combined restricted assets for our regulated subsidiaries were \$40,545 and \$53,592 as of December 31, 2018 and 2017, respectively.

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26. Supplementary Information on Cash Flow Activities

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Supplementary information			
Noncash transactions affecting cash flow activities			
Change in net unrealized (gain) loss on securities available for sale, including deferred income tax liability (asset) of (\$1,870), \$3,846, and \$1,085 in 2018, 2017, and 2016, respectively	\$ 9,048	\$ (13,867)	\$ 107
Change in liability for pension benefits, and deferred income tax (asset) liability of \$457, (\$3,202), \$10,792, in 2018, 2017, and 2016, respectively	\$ (738)	\$ 5,008	\$ (16,879)
Repurchase and retirement of common stock	\$ (748)	\$ (89)	\$ (56)
Exercise of stock options	\$ -	\$ -	\$ 55
Other			
Income taxes paid	\$ 8,978	\$ 10,363	\$ 11,549
Interest paid	\$ 6,903	\$ 6,794	\$ 7,635

27. Segment Information

The operations of the Company are conducted principally through three reportable business segments: Managed Care, Life Insurance, and Property and Casualty Insurance. Reportable business segments were identified according to the type of insurance products offered and consistent with the information provided to the chief operating decision maker. These segments and a description of their respective operations are as follows:

- **Managed Care segment** – This segment is engaged in the sale of managed care products to the Commercial, Medicare and Medicaid market sectors. The Commercial accounts sector includes corporate accounts, U.S. federal government employees, individual accounts, local government employees, and Medicare supplement. The following represents a description of the major contracts by sector:
 - The segment is a qualified contractor to provide health coverage to federal government employees within Puerto Rico and the USVI. Earned premiums revenue related to this contract amounted to \$150,232, \$156,417 and \$163,556 for the years ended December 31, 2018, 2017, and 2016, respectively (see note 12).
 - Under its commercial business, the segment also provides health coverage to certain employees of the Commonwealth of Puerto Rico and its instrumentalities. Earned premium revenue related to such health plans amounted to \$24,186, \$28,149 and \$29,475 for years ended December 31, 2018, 2017, and 2016, respectively.
 - The segment provides services through its Medicare health plans pursuant to a limited number of contracts with CMS. Earned premium revenue related to the Medicare business

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amounted to \$1,130,226, \$1,035,285, and \$1,023,904 for the years ended December 31, 2018, 2017, and 2016, respectively.

- The segment also participates in the Medicaid program to provide health coverage to medically indigent citizens in Puerto Rico, as defined by the laws of the government of Puerto Rico. Earned premium revenue related to this business amounted to \$776,038, \$751,393, and \$783,231 for the years ended December 31, 2018, 2017, and 2016, respectively.
- **Life Insurance segment** – This segment offers primarily life and accident and health insurance coverage, and annuity products. The premiums for this segment are mainly subscribed through an internal sales force and a network of independent brokers and agents.
- **Property and Casualty Insurance segment** – The predominant insurance products of this segment commercial package, commercial auto, and personal package. The premiums for this segment are originated through a network of independent insurance agents and brokers. Agents or general agencies collect the premiums from the insureds, which are subsequently remitted to the segment, net of commissions. Remittances are generally due 60 days after the closing date of the general agent's account current.

The Company evaluates performance based primarily on the operating revenues and operating income of each segment. Operating revenues include premiums earned (net), administrative service fees and net investment income. Operating costs include claims incurred and operating expenses. The Company calculates operating income or loss as operating revenues less operating costs.

The accounting policies for the segments are the same as those described in the summary of significant accounting policies included in the notes to consolidated financial statements. The financial data of each segment is accounted for separately; therefore, no segment allocation is necessary. However, certain operating expenses are centrally managed, therefore requiring an allocation to each segment. Most of these expenses are distributed to each segment based on different parameters, such as payroll hours, processed claims, or square footage, among others. In addition, some depreciable assets are kept by one segment, while allocating the depreciation expense to other segments. The allocation of the depreciation expense is based on the proportion of assets used by each segment. Certain expenses are not allocated to the segments and are kept within TSM's operations.

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The following tables summarize the operations by operating segment for each of the years in the three-year period ended December 31:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Operating revenues			
Managed care			
Premiums earned, net	\$ 2,687,773	\$ 2,588,692	\$ 2,647,169
Fee revenue	14,701	16,514	17,843
Intersegment premiums/fee revenue	5,690	6,362	5,918
Net investment income	23,827	16,659	15,102
Total managed care	<u>2,731,991</u>	<u>2,628,227</u>	<u>2,686,032</u>
Life			
Premiums earned, net	167,888	161,628	156,140
Intersegment premiums	668	218	716
Net investment income	25,658	24,819	24,877
Total life	<u>194,214</u>	<u>186,665</u>	<u>181,733</u>
Property and casualty			
Premiums earned, net	82,930	76,612	87,332
Intersegment premiums	613	613	613
Net investment income	10,800	9,489	8,891
Total property and casualty	<u>94,343</u>	<u>86,714</u>	<u>96,836</u>
Other segments*			
Intersegment service revenues	283	8,677	9,907
Operating revenues from external sources	5,794	3,763	3,563
Total other segments	<u>6,077</u>	<u>12,440</u>	<u>13,470</u>
Total business segments	3,026,625	2,914,046	2,978,071
TSM operating revenues from external sources	1,624	545	19
Elimination of intersegment premiums	(6,971)	(7,193)	(7,247)
Elimination of intersegment service revenue	(283)	(8,677)	(9,907)
Other intersegment eliminations	-	-	(78)
Consolidated operating revenues	<u>\$ 3,020,995</u>	<u>\$ 2,898,721</u>	<u>\$ 2,960,858</u>

* Includes segments that are not required to be reported separately, primarily the data processing services organization and the health clinics.

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	<u>2018</u>	<u>2017</u>	<u>2016</u>
Operating income (loss)			
Managed care	\$ 26,468	\$ 55,040	\$ (36,777)
Life	19,901	19,434	21,458
Property and casualty	(110,119)	(6,034)	12,074
Other segments*	8	(391)	(1,784)
Total business segments	<u>(63,742)</u>	<u>68,049</u>	<u>(5,029)</u>
TSM operating revenues from external sources	1,624	545	19
TSM unallocated operating expenses	(8,815)	(9,787)	(9,739)
Elimination of TSM charges	<u>9,600</u>	<u>9,600</u>	<u>9,522</u>
Consolidated operating (loss) income	(61,333)	68,407	(5,227)
Consolidated net realized investment gains	298	10,831	17,379
Consolidated net unrealized investment losses on equity securities	(36,546)	-	-
Consolidated interest expense	(6,903)	(6,794)	(7,635)
Consolidated other income, net	<u>11,312</u>	<u>6,533</u>	<u>6,569</u>
Consolidated (loss) income before taxes	<u>\$ (93,172)</u>	<u>\$ 78,977</u>	<u>\$ 11,086</u>
	<u>2018</u>	<u>2017</u>	<u>2016</u>
Depreciation and amortization expense			
Managed care	\$ 10,525	\$ 10,007	\$ 11,114
Life	1,134	1,203	1,030
Property and casualty	384	528	544
Other segments*	705	673	645
Total business segments	<u>12,748</u>	<u>12,411</u>	<u>13,333</u>
TSM depreciation expense	<u>787</u>	<u>787</u>	<u>787</u>
Consolidated depreciation and amortization expense	<u>\$ 13,535</u>	<u>\$ 13,198</u>	<u>\$ 14,120</u>

* Includes segments that are not required to be reported separately, primarily the data processing services organization and the health clinics.

Triple-S Management Corporation and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2018, 2017, and 2016

(dollar amounts in thousands)

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Assets			
Managed care	\$ 1,078,262	\$ 1,092,715	\$ 1,013,872
Life	863,470	853,289	816,920
Property and casualty	747,583	1,094,773	349,159
Other segments*	20,705	19,027	26,034
Total business segments	<u>2,710,020</u>	<u>3,059,804</u>	<u>2,205,985</u>
Unallocated amounts related to TSM			
Cash, cash equivalents, and investments	57,818	81,169	17,033
Property and equipment, net	21,733	22,257	22,380
Other assets	22,521	22,763	21,646
	<u>102,072</u>	<u>126,189</u>	<u>61,059</u>
Elimination entries – intersegment receivables and others	<u>(51,844)</u>	<u>(69,228)</u>	<u>(48,045)</u>
Consolidated total assets	<u>\$ 2,760,248</u>	<u>\$ 3,116,765</u>	<u>\$ 2,218,999</u>
	<u>2018</u>	<u>2017</u>	<u>2016</u>
Significant noncash items			
Net change in unrealized gain (loss) on securities available for sale			
Managed care	\$ 2,585	\$ 3,932	\$ 104
Life	(11,285)	7,142	2,659
Property and casualty	(583)	2,691	(2,984)
Other segments*	-	-	105
Total business segments	<u>(9,283)</u>	<u>13,765</u>	<u>(116)</u>
Amount related to TSM	<u>235</u>	<u>102</u>	<u>9</u>
Consolidated net change in unrealized (loss) gain on securities available for sale	<u>\$ (9,048)</u>	<u>\$ 13,867</u>	<u>\$ (107)</u>

* Includes segments that are not required to be reported separately, primarily the data processing services organization and the health clinics.

28. Subsequent Events

The Company evaluated subsequent events through the date the consolidated financial statements were issued. No events, other than those described in these notes, have occurred that require adjustment or disclosure pursuant to current Accounting Standard Codification.

Shareholder **Information**

Corporate Headquarters

Triple-S Management Corporation
1441 F. D. Roosevelt Avenue
San Juan, PR 00920
787.749.4949
www.triplesmanagement.com

Form 10-K

The company has filed an Annual Report on Form 10-K for the year ended December 31, 2018, with the Securities and Exchange Commission (SEC).

Triple-S Management Corporation's Annual Report and other SEC filings may be accessed at sec.gov or at triplesmanagement.com, Investor Relations section, SEC Filings Documents link.

Investor Relations

Garrett Edson
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787.792.6488
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At the company:

Juan J. Román-Jiménez
Executive Vice President and
Chief Financial Officer (CFO)
787.749.4949
jjroman@ssspr.com

Notice of Annual Meeting

The Annual Meeting of Shareholders will be held on April 26th, 2019 at 9:00 a.m. local time at Triple-S Management Corporation headquarters located at 1441 F.D. Roosevelt Avenue, San Juan, Puerto Rico.

Independent Registered Public Accounting Firm

Deloitte & Touche LLP
350 Chardón Avenue
Suite 700
San Juan, PR 00918-2140

Transfer Agent and Registrar

American Stock Transfer & Trust Company, LLC
6201 15th Avenue
Brooklyn, NY 11219
All Shareholder Inquiries: 800.937.5449
Shareholder Services: 718.921.8124
TTY: 718.921.8386 or 866.703.9077
www.amstock.com

Class B Common Stock

The company's common stock is listed on the New York Stock Exchange (NYSE) under the symbol "GTS."

Annual Certifications

Our President and Chief Executive Officer (CEO) has submitted to the NYSE the Domestic Company Section 303A Annual CEO Certification regarding our compliance with the corporate governance listing standards of the NYSE. In addition, we have filed with the SEC, as exhibits to our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, the Sarbanes-Oxley Act Section 302 Certifications of both our President and CEO and our Executive Vice President and CFO regarding the quality of our public disclosures.

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 **TRIPLE-S** MANAGEMENT

