American Family Insurance Mutual Holding Company and Subsidiaries

Consolidated Financial Statements
December 31, 2018 and 2017

Report of Independent Auditors

To the Board of Directors of American Family Insurance Mutual Holding Company:

We have audited the accompanying consolidated financial statements of American Family Insurance Mutual Holding Company and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of comprehensive income, of changes in members' equity, and of cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of American Family Insurance Mutual Holding Company and its subsidiaries as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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Other Matter

Accounting principles generally accepted in the United States of America require that the incurred and paid claims development tables for years prior to 2018 and the average annual percentage payout of incurred claims by age as of December 31, 2018 on pages 58 through 60 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PricewaterhouseCoopers LLP

March 1, 2019

American Family Insurance Mutual Holding Company and Subsidiaries
Consolidated Balance Sheets
Years Ended December 31, 2018 and 2017
(in thousands of dollars)

	2018	2017
Assets		
Bonds	$ 15,536,000	$ 13,572,740
Common stocks (including $2,310,538 and $2,588,998 at fair value)	2,368,958	2,646,816
Mortgage loans	715,372	687,606
Real estate	10,798	7,804
Policy loans	192,534	196,759
Cash and cash equivalents	747,365	687,166
Short-term investments	182,021	157,264
Other invested assets	1,238,061	997,651
Total cash and investments	20,991,109	18,953,806
Property & casualty premiums receivable and agents' balances	2,076,260	1,679,079
Accrued investment income	156,081	134,560
Deferred policy acquisition costs	905,631	797,153
Property and equipment (net of accumulated depreciation of $777,407 and $1,017,094)	903,024	785,329
Reinsurance recoverable	568,501	651,637
Prepaid reinsurance premium	104,277	98,509
Prepaid pension asset	242,777	—
Income tax recoverable	22,798	188,380
Deferred tax assets	144,097	—
Goodwill	561,878	329,792
Intangible assets	345,063	142,242
Other assets	195,411	141,502
Separate account assets	285,614	331,049
Total assets	27,502,521	24,233,038
Liabilities		
Property & casualty loss and loss adjustment expense reserve	6,430,892	4,750,962
Liabilities for life policies and deposit contracts	4,284,613	4,227,795
Property & casualty unearned premiums	4,553,512	3,673,494
Life policyholders' dividends payable	6,338	6,607
Deferred tax liabilities	—	64,064
Agent contract termination payments	780,233	762,347
Employee pension and other benefits	125,259	336,491
Debt (includes $606,920 and $647,566 at fair value)	813,365	814,005
Accrued expenses	337,524	335,103
Ceded premiums payable	67,055	72,829
Other liabilities	811,269	806,467
Separate account liabilities	285,614	331,049
Total liabilities	18,495,674	16,181,213
Members' equity		
Acquired capital	1,179,000	—
Retained earnings	7,648,682	7,469,170
Accumulated other comprehensive income (loss)	179,165	582,655
Total members' equity	9,006,847	8,051,825
Total liabilities and members' equity	$ 27,502,521	$ 24,233,038

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

American Family Insurance Mutual Holding Company and Subsidiaries
Consolidated Statements of Comprehensive Income
Years Ended December 31, 2018 and 2017
(in thousands of dollars)

	2018	2017
Revenues		
Property & casualty premiums earned	$ 8,927,496	$ 8,205,266
Life insurance premiums, fees, and other considerations	338,113	331,019
Net investment income	699,437	523,281
Net impairment losses recognized in earnings	(26,778)	(23,381)
Other realized capital gains (losses)	185,220	315,306
Other income	212,724	193,862
Total revenues	10,336,212	9,545,353
Benefits and expenses		
Property & casualty losses and loss adjustment expenses incurred	6,805,796	6,324,473
Life insurance claims and other benefits	210,713	191,961
Life insurance dividends to policyholders	12,266	14,781
Change in future life policy benefits	95,907	104,313
Other property & casualty underwriting expenses	2,515,386	2,485,671
Other expenses	374,046	275,126
Total benefits and expenses	10,014,114	9,396,325
Income (loss) before income tax expense (benefit)	322,098	149,028
Income tax expense (benefit)		
Current	(12,384)	(125,453)
Deferred	39,190	118,853
Total income tax expense (benefit)	26,806	(6,600)
Net income (loss)	295,292	155,628
Other comprehensive income (loss)		
Changes in unrealized gains and losses on securities (net of tax of ($212,293) and $120,941 and deferred policy acquisition cost adjustments of ($40,328) and $11,856 in 2018 and 2017, respectively)	(311,945)	336,732
Less: reclassification adjustment for net gains (losses) included in other realized capital gain (loss) (net of tax of $61,792 and ($48,825) in 2018 and 2017, respectively)	218,291	170,061
Changes in defined benefit obligations (net of tax of $6,283 and ($23,477) in 2018 and 2017, respectively)	10,966	(30,431)
Other comprehensive income (loss)	(519,270)	136,240
Comprehensive income (loss)	$ (223,978)	$ 291,868

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

American Family Insurance Mutual Holding Company and Subsidiaries
Consolidated Statements of Changes in Members' Equity
Years Ended December 31, 2018 and 2017
(in thousands of dollars)

	2018	2017
Acquired capital		
Balance at beginning of year	$ —	$ —
Equity from merger-See Note 2	1,179,000	—
Balance at end of year	1,179,000	—
Retained earnings		
Balance at beginning of year	7,469,170	7,313,542
Reclassification of certain tax effects (new accounting guidance)-See Note1(p)	(115,780)	—
Net income (loss)	295,292	155,628
Balance at end of year	7,648,682	7,469,170
Accumulated other comprehensive income (loss)		
Net unrealized gain (loss) on investments		
Balance at beginning of year	790,306	615,984
Reclassification of certain tax effects (new accounting guidance)	163,634	—
Change in unrealized gain (loss) on investments	(721,064)	250,643
Income tax benefit (expense)	159,255	(76,321)
Balance at end of year	392,131	790,306
Net unrealized gain (loss) on deferred acquisition costs		
Balance at beginning of year	(20,881)	(13,230)
Reclassification of certain tax effects (new accounting guidance)	(4,540)	—
Unrealized gain (loss) adjustments on deferred acquisition costs	40,328	(11,856)
Income tax benefit (expense)	(8,755)	4,205
Balance at end of year	6,152	(20,881)
Pension and other post-retirement benefit obligations		
Balance at beginning of year	(186,770)	(156,339)
Reclassification of certain tax effects (new accounting guidance)	(43,314)	—
Change in pension and other post-retirement benefit obligations	17,249	(53,908)
Income tax benefit (expense)	(6,283)	23,477
Balance at end of year	(219,118)	(186,770)
Total accumulated other comprehensive income (loss)	179,165	582,655
Total members' equity	$ 9,006,847	$ 8,051,825

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

American Family Insurance Mutual Holding Company and Subsidiaries
Consolidated Statements of Cash Flows
Years Ended December 31, 2018 and 2017
(in thousands of dollars)

	2018	2017
Cash flows from operating activities		
Net income (loss)	$ 295,292	$ 155,628
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities		
Depreciation, amortization, and other noncash items	279,232	247,014
Fair value option of long-term debt	(40,646)	45,711
Net realized (gains) losses on sales of property and equipment	264	(356)
Net realized (gains) losses on sales of investments	(158,842)	(292,069)
Change in value of derivatives	(8,517)	4,737
Earnings of equity method investments	32,773	(60,848)
Change in unearned premiums	275,187	219,585
Change in deferred policy acquisition costs	(68,151)	(45,521)
Change in deferred income tax provision	39,777	118,674
Change in insurance reserves	642,569	748,494
Change in reinsurance recoverable	140,257	(400,771)
Change in income tax receivable	164,012	(176,020)
Change in pension and postretirement benefit obligations	(459,609)	(24,214)
Other changes in operating assets and liabilities	(135,493)	(134,031)
Net cash provided by (used in) operating activities	998,105	406,013
Cash flows from investing activities		
Proceeds from sales, maturities, or calls of bonds	11,973,203	10,674,332
Purchases of bonds	(12,795,604)	(10,864,802)
Proceeds from sales of common stocks	1,276,647	1,432,013
Purchases of common stocks	(946,187)	(1,265,845)
Proceeds from collections on mortgage loans	77,158	86,185
Purchases of mortgage loans	(104,924)	(198,623)
Proceeds from sales of other investments	242,082	761,085
Purchases of other investments	(348,523)	(877,093)
Net purchases and sales of short-term investments	(7,228)	(42,906)
Acquisition, net of cash acquired	—	(123,837)
Cash acquired in merger	24,573	—
Net purchases and sales of property and equipment	(190,479)	(166,655)
Other investing activities	3,475	8,342
Net cash provided by (used in) investing activities	(795,807)	(577,804)
Cash flows from financing activities		
Deposits to investment-type and universal life contracts	74,070	76,477
Withdrawals from investment-type and universal life contracts	(86,169)	(86,704)
Net proceeds (repayments) of Federal Home Loan Bank advances	(130,000)	130,000
Net cash provided by (used in) financing activities	(142,099)	119,773
Net change in cash and cash equivalents	60,199	(52,018)
Cash and cash equivalents		
Beginning of year	687,166	739,184
End of year	$ 747,365	$ 687,166
Income taxes paid (received)	$ (189,480)	$ 50,524
Interest paid (received)	31,828	27,600

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

1. Nature of Operations and Significant Accounting Policies

American Family Insurance Mutual Holding Company (AFI MHC) and its wholly-owned subsidiaries, primarily American Family Mutual Insurance Company, S.I. (AFMICSI), are engaged principally in the writing of property & casualty and life insurance policies within the United States and distribute products through agency and direct sales channels. On January 1, 2017, both AFI MHC and its wholly-owned subsidiary, AmFam Holdings, Inc. (Holdings), the 100% owner of AFMICSI, were created as part of a corporate reorganization. Additionally, as part of the corporate reorganization, American Family Mutual Insurance Company (AFMIC) was converted to AFMICSI through the issuance of common stock to Holdings. AFI MHC and its consolidated subsidiaries are herein referred to collectively as the “Companies” or the “Company.”

The Company's exclusive agency sales distribution channel primarily sells personal lines and commercial products predominantly through an agency force in a nineteen state operating territory.

Exclusive agents also sell life insurance products, which are underwritten by American Family Life Insurance Company (AFLIC), including term, whole, and universal life insurance policies. AFLIC is licensed to sell policies in 49 states and the District of Columbia.

Personal lines policies are also sold through a direct sales distribution channel by PGC Holdings Corp. and its subsidiaries (PGC) and Homesite Group, Inc. and its subsidiaries (Homesite). PGC is licensed to sell policies in 49 states and the District of Columbia. Homesite is licensed to sell policies in all 50 states and the District of Columbia.

The Company also sells commercial and personal lines policies through an independent agency sales distribution channel through its subsidiary, Main Street America Group, Inc. (MSAG), which merged with AFI MHC on October 31, 2018 (See Note 2 for further information on the accounting for this business combination).

Property & casualty insurance premiums represented 96% of total net premiums written for both 2018 and 2017.

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) which require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Significant accounting policies used in the preparation of these consolidated financial statements include:

a. Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Companies after elimination of all significant intercompany balances and activities.

b. Cash and Investments

Cash and cash equivalents represent cash and securities that have maturities of three months or less at purchase and consist primarily of money market mutual funds carried at cost, which approximates fair value. Short-term investments represent securities that have maturities of one year or less at purchase and are accounted for in the same manner as long-term bonds.

The Companies may dispose of bonds prior to their scheduled maturity due to changes in market interest rates, tax and credit considerations, liquidity or regulatory capital requirements, or other similar factors. As a result, the Companies consider all bonds and common stocks available-for-sale with the exception of certain bonds which are considered trading securities and certain common stock positions valued using the cost or equity method. Available-for-sale investments are reported at fair value, with unrealized gains and losses, net of applicable deferred taxes, reported as a component of accumulated other comprehensive income until realized. If there is a decline in an investment's net realizable value that is other-than-temporary, the decline is recorded as a realized loss and the book value of the investment is reduced to its fair value or present value of expected future cash flows.

The Company also invests in to-be-announced securities (TBAs), which are investments in forward-dated mortgage-backed securities. Each TBA position is disposed of before the trade settlement date as part of an income generation strategy. All TBA purchase and sale activity is recorded on the trade date, and all cash is settled on a gross basis.

The Company initiates its positions in TBAs through both purchases and sales. Positions outstanding as of the end of the year that were initiated through purchases are classified as bonds, available-for-sale in the consolidated balance sheets. Purchase and sale activity of these long positions is included with purchases of bonds and proceeds from sales, maturities, or calls of bonds, respectively, in the consolidated statements of cash flows. Any initial sales are referred to as "short sales" and represent obligations to deliver the applicable TBA(s) by the settlement date. Positions outstanding as of the end of the year that were initiated through short sales are classified as securities sold, not yet purchased within other liabilities in the consolidated balance sheets. Purchase and sale activity of these short sale positions is included within purchases of other investments and proceeds from sales of other investments, respectively, in the consolidated statements of cash flows.

Other invested assets consist primarily of investments in limited partnerships. The limited partnerships are reported in the consolidated financial statements according to the Company's percentage of equity ownership in the limited partnerships. The Company has determined an ownership percentage of 5% or greater is more than a minor interest in a limited partnership, and these investments are accounted for using the equity method of accounting. The cost method of accounting is used to account for limited partnerships with a less than 5% ownership interest, as the Company's interest is so minor that it exercises virtually no influence over the investee's operations. Due to the nature and structure of these cost method investments, they do not meet the characteristics of an equity security in accordance with applicable accounting standards. These investments typically reflect a reporting lag of up to three months, dependent upon receipt of the limited partnership financial statements. The Company also holds low income housing tax credits that are recorded at amortized cost and federal historic tax credits which are recorded at the audited equity values.

For the limited partnerships accounted for under the equity method of accounting, all income from these partnerships, including net investment income, realized capital gains and losses, and changes in unrealized gains and losses, is recorded as net investment income on the consolidated statements of comprehensive income.

Derivative instruments are accounted for on a fair value basis and reported as other assets or other liabilities, as applicable, on the consolidated balance sheets. When certain derivatives meet specific criteria, they may be designated as accounting hedges and accounted for as fair value, cash flow, or foreign currency hedges. The Company did not elect to apply hedge accounting for the derivative instruments that were utilized during the reporting period. As a result, unrealized gains and losses on open derivative positions are recognized as a component of net investment income, with an adjustment to the carrying value of the derivative instrument. Interim settlements involving the receipt or payment of cash as well as the gain or loss recognized upon exiting a derivative position are also included as a component of net investment income. Cash flows from derivatives are reported in cash flows from investing activities within the consolidated statements of cash flows.

Prepayment assumptions for mortgage-backed and asset-backed securities are obtained from external sources when the securities are purchased. These allow the Company to recognize income using a constant effective yield based on those prepayment assumptions and the economic life of the securities. Updated prepayment assumptions are obtained on a monthly basis, and the effective yield is recalculated to reflect actual payments received and expected future payments.

Real estate assets consist of land, buildings, and building improvements held for the production of income. Land is reported at cost. Buildings and improvements are carried at cost, less accumulated depreciation computed on the straight-line method over estimated useful lives ranging from twenty to forty-five years.

Mortgage loans are carried at their aggregate unpaid principal balances, net of a valuation allowance for estimated uncollectible amounts. Policy loans are reported at their outstanding principal balance and are limited to the cash value of the policy.

Common stocks are generally reported in the consolidated financial statements at fair value, which is based primarily on values published by independent pricing sources and quoted market prices.

Investment income is recorded when earned. Dividend income is recorded on the ex-dividend date. Realized gains and losses on sales of investments are determined on a specific identification basis and are recorded in the accompanying consolidated statements of comprehensive income.

c. Fair Value Measurements

Financial assets and financial liabilities recorded on the consolidated balance sheets at fair value are categorized based on the reliability of inputs to the valuation techniques as follows:

Level 1 Financial assets and financial liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Company can access.

Level 2 Financial assets and financial liabilities whose values are based on the following:
Quoted prices for similar assets or liabilities in active markets;
Quoted prices for identical or similar assets or liabilities in non-active markets; or
Valuation models whose inputs are observable, directly or indirectly, for substantially the full term of the asset or liability.

Level 3 Financial assets and financial liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs may reflect the Company's estimates of the assumptions that market participants would use in valuing the financial assets and financial liabilities.

The availability of observable inputs varies by instrument. In situations where fair value is based on internally developed pricing models or inputs that are unobservable in the market, the determination of fair value requires more judgment. In many instances, inputs used to measure fair value fall into different levels of the fair value hierarchy. In those instances, for disclosure purposes, the level in the fair value hierarchy within which the fair value measurement is categorized is determined based on the lowest level of input that is significant to the fair value measurement in its entirety.

d. Premiums Written on Property & Casualty Insurance and Life Insurance

Property & casualty premiums written are recorded on the effective date of the contract and earned on a pro rata basis over the terms of the policies. Premiums earned include premiums assumed and are presented net of premiums ceded under various reinsurance contracts. Unearned premium represents the portion of written premium applicable to the unexpired portion of insurance in-force. Advance premium represents amounts received prior to policy effective dates. Premiums receivable and agents' balances are net of an allowance for doubtful accounts of $13,167 and $10,614 at December 31, 2018 and 2017, respectively.

The Company considers an account delinquent if payment is not received according to the contractual terms of the related insurance policy. Typically, accounts are charged off after attempts to collect the funds are exhausted by internal and external sources. The Company generally does not charge interest on delinquent accounts.

The Company annually evaluates whether a premium deficiency exists relating to short- and long-duration contracts. Anticipated investment income is considered as part of this evaluation. A premium deficiency reserve of $20,575 and $23,970 was recorded as of December 31, 2018 and 2017, respectively.

Term life and whole life insurance premiums are generally recognized as premium income when received. Benefits and expenses are associated with earned premiums so as to result in recognition of profits over the life of the contracts. The association is accomplished by means of the provision for liabilities for future policy benefits and the amortization of deferred policy acquisition costs (see Note 1(e)). Premium income is recorded net of premiums ceded to reinsurers. Commissions and other expenses are recorded net of allowances received from reinsurers.

For investment-type and universal life insurance contracts, premium deposits and benefit payments are recorded as increases or decreases in a liability account, rather than as revenue and expense. Revenue is recognized for any amounts charged against the liability account for the cost of insurance, policy administration, and surrender penalties. Expense is recorded for any interest credited to the liability account and any benefit payments which exceed the contract liability account balance.

e. Deferred Policy Acquisition Costs (DAC)

Costs that are directly related to the successful acquisition of new or renewal insurance contracts are deferred to the extent that such costs are deemed recoverable. These costs include, but are not limited to, commissions, certain costs of policy issuance and underwriting, and certain agency expenses. All other acquisition costs are expensed as incurred. For property & casualty contracts, deferred costs are amortized as the related premiums are earned. For term life insurance contracts, deferred costs are amortized with interest in relation to future anticipated premium revenue, using the same assumptions that are used in calculating the insurance liabilities. For traditional whole life insurance contracts, deferred costs are amortized in relation to the present value of expected gross margins, discounted using the interest rate earned on the underlying assets. For deposit contracts without significant mortality risk (investment-type contracts) and for contracts that permit the Company or the policyholder to make changes in the contract terms (universal life insurance contracts), deferred costs are amortized in relation to the present value of expected gross profits from these contracts, discounted using the interest rate credited to the policy or the expected earnings rate, depending on the type of policy.

The Companies regularly evaluate the recoverability of the unamortized balance of DAC. For property & casualty insurance, if DAC were to exceed the sum of unearned premiums and related anticipated investment income less expected losses and loss adjustment expenses and policy maintenance costs, the excess cost would be expensed immediately. For term life insurance contracts, the unamortized asset balance is reduced by a charge to income only when the estimated remaining gross premium reserve exceeds the GAAP reserves reduced by unamortized DAC. For traditional whole life insurance contracts, the accumulated amortization is adjusted (whether an increase or a decrease) whenever there is a material change in the estimated gross margins expected over the life of a block of business in order to maintain a constant relationship between the cumulative amortization and the present value (discounted at the rate of interest earned on the underlying assets) of expected gross margins. For universal life and investment-type insurance contracts, the accumulated amortization is adjusted (whether an increase or a decrease) whenever there is a material change in the estimated gross profits expected over the life of a block of business in order to maintain a constant relationship between the cumulative amortization and the present value of expected gross profits.

DAC is also adjusted when bonds are recorded at fair value for traditional whole life, universal life, and investment-type insurance contracts. This adjustment, which is recorded as part of the net appreciation (depreciation) of securities in accumulated other comprehensive income, reflects the change in cumulative amortization that would have been recorded if these bonds had been sold at their fair values and the proceeds were reinvested at current yields.

f. Property & Casualty Loss and Loss Adjustment Expense Reserve

The property & casualty loss and loss adjustment expense reserve includes amounts determined on the basis of claim evaluation and other estimates for reported losses, and includes estimates for losses incurred but not reported and anticipated salvage and subrogation recoveries (health insurance does not include salvage). These estimates are continually reviewed and updated and any adjustments are charged to income as incurred.

Reinsurance recoveries are recorded as a reduction of losses and loss adjustment expenses in accordance with contract terms. The liability for gross long-term care claims has been discounted on a tabular basis using morbidity from industry data including the Society of Actuaries Long-Term Care Experience Studies with a discount rate that varies by claim incurred year, which has been 3.5% since 2013. The liabilities include $16,799 and $13,715 of such discounted reserves at December 31, 2018 and 2017, respectively.

Due to the reasonably complex and dynamic process of establishing these reserves, which can be influenced by a variety of factors and assumptions, actual ultimate losses and loss adjustment expenses which may emerge in future years may vary materially from the amounts recorded in these consolidated financial statements.

g. Liabilities for Life and Deposit-Type Contracts

For term life insurance contracts, reserves are calculated using the net level premium method, based on assumptions as to investment yields, mortality, withdrawals, expenses, and policyholder dividends. These assumptions are made at the time the contract is issued and are consistent with assumptions used in the product pricing process. Assumptions are based on projections from past experience and are modified only as necessary to reflect loss recognition. In addition, an allowance is made for possible unfavorable deviations from selected assumptions.

For traditional whole life insurance contracts, reserves are calculated based on the net level policy benefit reserve. Interest assumptions are consistent with the policy dividend formula and mortality assumptions are based on the 1958, 1980, or 2001 CSO table. The interest rate on current issues is between 3.5% and 4.0% in 2018 and was 4.0% in 2017. Interest rates on all other issues are between 2.5% and 5.0% in both 2018 and 2017.

For universal life, deposit-type and investment-type insurance contracts, reserves are based on the contract account balance. Reserves for annuities in payout status are calculated as the present value of future benefits using contract interest rates and either the 1971, 1983 or 2000 Immediate Annuity Mortality table.

(in thousands of dollars)

Gross reserves by type of contract at December 31 are as follows:

	2018		2017	
Insurance-type liabilities				
Traditional whole life	$ 2,609,549	60.8%	$ 2,545,528	60.1%
Traditional term life	481,496	11.2	478,462	11.3
Payout annuities	45,213	1.1	44,920	1.1
Other insurance reserves	9,779	0.2	9,358	0.2
Deposit-type liabilities				
Universal life	500,348	11.7	497,926	11.8
Deferred annuities	267,010	6.2	269,259	6.4
Dividend accumulations	233,826	5.5	236,072	5.6
Structured settlements	33,632	0.8	36,921	0.9
Variable universal life	16,172	0.4	16,363	0.4
Variable annuities	14,997	0.4	14,432	0.3
Supplemental contracts without life contingencies, retained assets and premium deposits	72,591	1.7	78,554	1.9
Total liabilities for life policies and deposit contracts	$ 4,284,613	100.0%	$ 4,227,795	100.0%

h. Life Policyholders Dividends Payable

Approximately 97.5% of the Company's life contracts are considered participating policies. The Company accounts for policyholder dividends based upon dividend scales approved by AFLIC's Board of Directors. The amount of dividends to be paid is determined annually. Participating policyholders generally have the option to direct their dividends to be paid in cash, used to reduce future premiums due, used to purchase additional insurance benefits, or left on deposit with the Company to accumulate interest. Dividends used by policyholders to purchase additional insurance benefits are reported as premiums in the consolidated statements of comprehensive income. The Company's annual declaration includes a guarantee of a minimum aggregate amount of dividends to be paid to policyholders as a group in the subsequent year. The portion of the Company's earnings allocated as dividends is included in policyholders' dividends payable.

i. Reinsurance

In the normal course of business, the Companies seek to limit exposure to loss on any single insured and to certain aggregate loss limits. This is accomplished by ceding insurance to other insurance companies or reinsurers under quota share, excess of loss, and coinsurance contracts. Liabilities related to insurance contracts are reported gross of the effects of reinsurance. Estimated reinsurance recoverable is recognized in a manner consistent with the liabilities related to the underlying reinsured contracts.

(in thousands of dollars)

Amounts ceded under reinsurance contracts as of and for the years ended December 31 are summarized as follows:

	2018	2017
Property & casualty reinsurance		
Earned premiums	$ 180,100	$ 160,603
Gross written premiums	174,680	216,527
Unearned premiums	108,390	98,563
Loss and loss adjustment expenses	294,950	455,977
Life reinsurance		
Premiums	76,113	76,212
Reserves	231,251	225,468
Commissions and expense allowances	23,762	23,877
Accident & health insurance benefits on ceded claims	44,398	30,849

AFLIC cedes 100% of its variable universal life (VUL) and variable annuity (VA) business, which AFLIC no longer sells, under a reinsurance agreement with a third party (see Note 13).

The Companies assume property reinsurance in order to diversify the Companies' geographic risk. Property & casualty earned premiums assumed under reinsurance contracts under this program during 2018 and 2017 were $264,970 and $186,820, respectively. Written premiums assumed during 2018 and 2017 were $269,253 and $198,790, respectively.

The Company does not enter into finite reinsurance contracts; all reinsurance contracts involve a significant transfer of risk. Ceded reinsurance transactions do not relieve the Company of its primary obligation to the policyholder.

j. Income Taxes

The Companies file a consolidated federal income tax return and are subject to a tax allocation agreement under which each member's tax liability equals or approximates separate return calculations with current credit for net losses and tax credits utilized by other members of the group. Deferred taxes are established for the future tax effects of temporary differences between the tax and financial reporting bases of assets and liabilities using currently enacted tax rates. The effect on deferred taxes of a change in tax rates is recognized in income in the period of enactment as a component of income tax expense from continuing operations. Deferred tax assets (DTAs) are valued based upon the expectation of future realization on a "more likely than not" basis. A valuation allowance is established for that portion of DTAs which cannot meet this realization standard. Based on all available evidence, a federal valuation allowance is not needed as of December 31, 2018 and 2017.

k. Property and Equipment

Property and equipment, including capitalized software, is carried at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, ranging from three to forty-five years.

The Company reviews fixed assets for impairment when there is reason to believe that a fixed asset's carrying value might not be recoverable, and charges any impairments to earnings.

(in thousands of dollars)

The gross cost, accumulated depreciation, and net cost of major classes of property and equipment as of December 31 are as follows:

	2018			2017		
	Gross Cost	Accumulated Depreciation	Net	Gross Cost	Accumulated Depreciation	Net
Property occupied by the Company	$ 606,513	$ (278,081)	$ 328,432	$ 535,471	$ (261,514)	$ 273,957
Furniture and equipment	166,637	(94,157)	72,480	211,527	(137,749)	73,778
Computer software and equipment	907,281	(405,169)	502,112	1,055,425	(617,831)	437,594
	$ 1,680,431	$ (777,407)	$ 903,024	$ 1,802,423	$ (1,017,094)	$ 785,329

Property occupied by the Company is inclusive of construction in progress of $25,837 and $24,969 at December 31, 2018 and 2017, respectively.

l. Goodwill

Goodwill represents the excess of cost over the fair value of net assets acquired in business combinations. Goodwill is not amortized, but is reviewed for impairment at least annually and whenever there is an impairment indicator, using a fair value based approach.

m. Intangible Assets

The establishment of intangible assets and the determination of estimated useful lives are primarily based on valuations received from qualified independent appraisers as a result of the Company's acquisition activity. The calculations of these amounts are based on estimates and assumptions using historical and pro forma data and recognized valuation methods. Different estimates or assumptions could produce different results. Contractual or separable intangible assets that have finite useful lives are amortized against income over their estimated useful lives using either the straight-line method or a weighted-average method based on projected pre-tax income generated by the intangible asset. Indefinite-lived intangible assets are not subject to amortization.

The Company evaluates the remaining useful lives of its intangible assets with a finite life at least annually to determine whether events or circumstances warrant a revision to the remaining period of amortization. The Company evaluates its indefinite-lived intangible assets for impairment on at least an annual basis. The Company evaluates its finite-lived intangible assets for impairment when circumstances indicate impairment may have occurred.

See Note 7 for more information on intangible assets.

n. Leases

The Company leases various office equipment and real estate under noncancelable operating lease agreements with various expiration dates through 2023 and thereafter. Lease expense for 2018 and 2017 was $48,370 and $44,694, respectively.

(in thousands of dollars)

As of December 31, 2018, the minimum aggregate lease commitments were as follows:

Year ending December 31	Operating Leases
2019	$ 51,566
2020	41,133
2021	34,975
2022	28,945
2023 and thereafter	67,653
Total	$ 224,272

Certain lease commitments have renewal options extending through the year 2036. Some of these renewals are subject to adjustments in future periods.

o. Separate Accounts

Separate account assets include segregated funds invested by the Company as designated by VUL and VA policy owners in shares of mutual funds managed by outside fund managers offered as investment vehicles for American Family Variable Accounts I or II. Policy owners are the only persons having rights to any assets in the separate accounts or to income arising from such assets. The assets (investments) and liabilities (to policy owners) of each account are clearly identifiable and distinguishable from other assets and liabilities of the Company. Assets are valued at fair value based on quoted market prices of the underlying funds, which are traded in non-active markets. The liabilities are equal to the amount due to the policy owner without a reduction for surrender charges. The net investment experience (investment income, gains and losses) of these accounts are credited directly to the policy owners and, therefore, are not included in the Company's net income.

p. Adoption of New Accounting Guidance

Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income

In February 2018, the Financial Accounting Standards Board (FASB) issued guidance that allows a reclassification of the stranded tax effects in accumulated other comprehensive income (AOCI) resulting from the Tax Cuts and Jobs Act of 2017 (the Act). The Company adopted this guidance on January 1, 2018 as a change in accounting policy. As a result, on January 1, 2018, the Company reclassified $115,780 of stranded tax effects which increased accumulated other comprehensive income and decreased retained earnings. This reclassification was solely due to the effect of the change in the federal tax rate on the Company's pension obligations and its net unrealized gain (loss) on investments and DAC.

Disclosure Requirements for Fair Value Measurement

In August 2018, the FASB issued guidance that modifies or eliminates certain disclosures related to fair value measurements. The changes are designed to improve the effectiveness of existing disclosures and eliminate disclosures that are not deemed cost beneficial. The guidance modifies disclosures related to purchases and issues of Level 3 assets and liabilities and eliminates disclosures related to transfers between Level 1 and Level 2 of the fair value hierarchy, the policy for timing of transfers between levels, valuation processes for Level 3 fair value measurements, and changes in unrealized gains and losses included in earnings for recurring Level 3 fair value measurements. The updated guidance is effective for reporting periods beginning after December 15, 2019, with early adoption permitted. The Company elected to early adopt this guidance as it affects disclosures only; therefore, the adoption of this guidance as of December 31, 2018 had no impact on the Company's financial position and results of operations.

(in thousands of dollars)

q. Statements of Cash Flows

Non-cash investing activities for the years ended December 31 are summarized as follows:

	2018	2017
Acquisitions of common stock	$ 40,421	$ 38,479
Disposals of common stock	54,588	35,484
Acquisitions of bonds	30,366	571,323
Disposals of bonds	30,366	578,650
Net acquisitions of short-term investments	—	4,468

After review of internal accounting policy in 2018, the Company determined non-cash acquisitions and disposals of bonds should only include transactions where the security acquired is significantly different than the security disposed. As it was impracticable to apply the updated policy retroactively, reported non-cash acquisitions and disposals of bonds are not comparable between years.

See Note 3(b) for non-cash investing activities in 2018 relating to charitable contributions of common stock and Note 2 for non-cash financing activities in 2018 relating to net assets acquired in a merger.

r. Reclassifications

Certain reclassifications have been made to prior year amounts in the accompanying consolidated financial statements to conform to current year presentation and allow for consistent financial reporting.

s. Subsequent Events

The Company has evaluated events subsequent to December 31, 2018 through March 1, 2019, the date these consolidated financial statements were available to be issued. Based on this evaluation, no events have occurred subsequent to December 31, 2018 that require disclosure or adjustment to the consolidated financial statements at that date or for the year then ended.

2. Business Combinations

Main Street America

On October 31, 2018, the Company merged with Main Street America Group Mutual Holdings, Inc. (MSAMHC), with MSAMHC ceasing to exist post-merger. Member interests in MSAMHC held by Main Street America policyholders were exchanged for member interests in AFI MHC, with no further consideration exchanged. The purpose of the merger is to diversify risk, promote growth through geographic and distribution channel expansion, and provide agents and policyholders with broader product offerings.

The transaction was accounted for under the acquisition method using MSAG historical financial information and applying fair value estimates to the acquired assets and liabilities as of the acquisition date. The excess fair value of the MSAG member interests acquired over the estimated fair value of the assets acquired, including intangible assets, and liabilities assumed at the acquisition date has been allocated to goodwill. The Company recognized $233,604 of goodwill, which is primarily attributable to an assembled workforce with industry-wide technical expertise and synergies that will bring increased value to customers through operating efficiencies.

(in thousands of dollars)

The following is a summary of the fair values of the tangible and intangible assets acquired and liabilities assumed at the date of acquisition.

		October 31, 2018
Assets		
Cash, cash equivalents and investments	$	2,209,428
Reinsurance recoverable		52,008
Premiums receivable		259,922
Intangible assets		241,180
Deferred tax assets		103,731
Other assets		129,142
Total assets		2,995,411
Liabilities		
Property & casualty loss and loss adjustment expense reserve		1,173,141
Property & casualty unearned premiums		605,283
Debt		170,195
Other liabilities		101,396
Total liabilities		2,050,015
Total identified net assets acquired	$	945,396
Goodwill		233,604
Acquired capital	$	1,179,000

The acquired intangible assets of $241,180 are comprised of independent agent and broker relationships, state insurance licenses, software, trade name and trademarks, value of business acquired, and renewal rights. Useful lives for finite-lived intangible assets related to the merger range from one to sixteen years. The goodwill will not be deductible for tax purposes.

Additionally, upon acquisition, the Company recorded fair value adjustments of $117,296 and $(3,976) related to property & casualty loss and loss adjustment expense reserves and reinsurance recoverables, respectively, both of which are presented net with (and reduce) the amounts recognized on the respective line items on the balance sheet and in the table above. These fair value adjustments are amortized over a period of seven years, and the net amortization expense of $7,144 is included within property & casualty losses and loss adjustment expenses incurred in the consolidated statements of comprehensive income for the year ended December 31, 2018.

As a result of the merger, the Company recorded $1,179,000 as equity from merger within acquired capital in the consolidated statements of changes in members' equity.

Acquisition related expenses of $16,238 were incurred by AFI MHC during 2018 and are included in other expenses in the consolidated statements of comprehensive income.

Networked Insights

On December 14, 2017, the Company acquired 100% of the ownership interest in Networked Insights, Inc. (NI), a data and analytics software company, for $131,696 in total consideration. NI was acquired to increase customer value through use of data, advanced analytics, and artificial intelligence.

(in thousands of dollars)

The transaction was accounted for under the acquisition method using NI historical financial information and applying fair value estimates to the acquired assets and liabilities as of the acquisition date. The excess of the purchase price over the estimated fair value of the assets acquired, including intangible assets, and liabilities assumed at the acquisition date has been allocated to goodwill. The Company recognized $93,278 of goodwill, which is primarily attributable to an assembled workforce with specialized technical expertise that will enhance the Company's digital transformation efforts.

The following is a summary of the fair values of the tangible and intangible assets acquired and liabilities assumed at the date of acquisition.

		December 14, 2017
Assets		
Cash and cash equivalents	$	6,146
Intangible assets		12,000
Deferred tax assets		21,092
Property and equipment		980
Other assets		547
Total assets		40,765
Liabilities		
Other liabilities		2,347
Total liabilities		2,347
Total identified net assets acquired	$	38,418
Goodwill	$	93,278

The acquired, finite-lived intangible assets of $12,000 were comprised of software and customer relationships and had useful lives of four and three years, respectively. Goodwill will not be deductible for tax purposes. In 2018, the Company recognized a measurement period adjustment resulting in a decrease to goodwill of $1,518.

Acquisition related expenses of $5,778 were incurred during 2017 and are included in other expenses in the consolidated statements of comprehensive income.

3. Financial Instruments

a. Fair Value of Financial Instruments

The fair value guidance establishes a hierarchy for inputs used in determining fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available.

Fair value is a market-based measure considered from the perspective of a market participant who owns an asset or owes a liability. Accordingly, when market observable data is not readily available, the Company's own assumptions are set to reflect those that market participants would be presumed to use in pricing the asset or liability at the measurement date. The Company uses prices and inputs that are current as of the measurement date, including during periods of market disruption. In periods of market disruption, the ability to observe prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified from one level of the hierarchy to another.

When available, the Company uses the market approach to estimate the fair value of its financial instruments, which is based on quoted prices in active markets that are readily and regularly available. Generally, these are the most liquid of the Company's holdings and valuation of these securities does not involve management judgment. Matrix pricing and other similar techniques are other examples of the market approach. Matrix pricing values a particular security by utilizing the prices of securities with similar ratings, maturities, industry classifications, and/or coupons and interpolating among known values of these similar instruments to derive a price.

When quoted prices in active markets are not available, the Company uses the income approach, or a combination of the market and income approaches, to estimate the fair value of its financial instruments. The income approach involves using discounted cash flow and other standard valuation methodologies. The inputs in applying these market standard valuation methodologies include, but are not limited to, interest rates, benchmark yields, bid/ask spreads, dealer quotes, liquidity, term to maturity, estimated future cash flows, credit risk and default projections, collateral performance, deal and tranche attributes, and general market data.

The following valuation techniques and inputs were used to estimate the fair value of each class of significant financial instruments:

Level 1 Measurements

Bonds: *U.S. Government*: Comprised of U.S. Treasuries valued based on unadjusted quoted prices for identical assets in active markets.

Common Stocks: Comprised of actively traded, exchange listed U.S. and international equity securities including mutual funds. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.

Cash Equivalents: Comprised of actively traded money market funds that have daily quoted net asset values for identical assets that the Company can access and U.S. Treasuries valued based on unadjusted quoted prices for identical assets in active markets.

Short-term Investments: Comprised of U.S. Treasuries with valuations based on unadjusted quoted prices for identical assets in markets that are generally active.

Level 2 Measurements

Bonds: The majority of the Company's Level 2 fixed income securities are priced by leading, nationally recognized providers of market data and analytics. These securities are principally valued using the market and income approaches. When available, recent trades of identical or similar assets are used to price these securities. However, because many fixed income securities do not actively trade on a daily basis, pricing models are often used to determine security prices. The pricing models discount future cash flows at estimated market interest rates. These rates are derived by calculating the appropriate spreads over comparable U.S. Treasury securities based on credit quality, industry, and structure of the asset. Observable inputs used by the models include benchmark yields, bid/ask spreads, dealer quotes, liquidity, term to maturity, credit risk and default projections, collateral performance, deal and tranche attributes, and general market data. Inputs may vary depending on type of security.

A small segment of Level 2 and Level 3 securities are priced internally using matrix pricing, broker quotes, and benchmark and spread analysis, or through third party vendors that specialize in difficult-to-price securities. Pricing for specific security types is as follows:

U.S. Government: Valued using the market and income approaches based on inputs including quoted prices for identical or similar assets in markets that are not active, benchmark yield curves, and bid/ask spreads.

Municipals: Valued using the market and income approaches based on inputs including quoted prices for identical or similar assets in markets that are not active, benchmark yield curves, bid/ask spreads, and credit quality.

Corporates, including privately placed: These securities are principally valued using the market and income approaches based on inputs including quoted prices for identical or similar assets in markets that are not active, or using matrix pricing or other similar techniques that use standard market observable inputs such as benchmark yield curves, bid/ask spreads, and credit quality. Privately placed securities are valued using internal matrix pricing and discounted cash flow methodologies using standard market observable inputs including taxable and tax-exempt yield curves and market observable ratings from external parties. Due to the relative illiquidity of private placements, illiquidity premiums of 25 and 100 basis points are factored into the yield curve inputs for investment grade and below investment grade securities, respectively.

Asset-Backed Securities (ABS), Residential Mortgage-backed Securities (RMBS), and Commercial Mortgage-backed Securities (CMBS): Valued using the market and income approaches based on inputs including quoted prices for identical or similar assets in markets that are not active, benchmark yield curves, bid/ask spreads, default assumptions, projected cash flows, collateral performance, deal structure, and tranche characteristics.

Common Stocks: Comprised of shares in the Federal Home Loan Banks of Chicago (FHLBC), Des Moines, and Indianapolis (collectively, FHLB). While not actively traded, the valuation for the FHLB investments is perpetually quoted at $100 per share by the FHLB.

Cash Equivalents: Cash equivalents are valued based on inputs including quoted prices for identical or similar assets in markets that are not active, benchmark yield curves, bid/ask spreads, and credit quality.

Short-term Investments: Short-term investments are valued based on quoted prices for identical or similar assets in markets that are not active, benchmark yield curves, bid/ask spreads, and credit quality.

Derivative Instruments: Over-the-counter (OTC) derivatives, including interest rate swaps, are valued using models that rely on inputs such as interest rate yield curves that are observable for substantially the full term of the contract. These models discount cash flows at each coupon date and the valuation of interest rate swaps is the difference between the values of the discounted cash flows of the fixed and floating legs of the swap. Fair value is the estimated amount that the Company would receive (pay) to terminate the derivative contracts at the reporting date. For some OTC derivative instruments including equity options, broker pricing is used. Derivative assets (liabilities) are reported gross of collateral payable (receivable) for purposes of fair value disclosures in Note 3(e).

Separate Account Assets: Comprised of mutual funds traded in non-active markets that have daily quoted net asset values for identical assets that the Company can access. Net asset values for the actively traded mutual funds in which the separate account assets are invested are obtained daily from the fund managers.

Debt: Comprised of an FHLBC fixed-rate advance, for which daily published interest rates are available. See Note 3(h) for additional valuation methodology.

Level 3 Measurements

Bonds:

Municipals: Valued internally using a discounted cash flow model and par value and externally using broker quotes.

Corporates: Valued using cash flow modeling and the mid-point of actual bid and ask market quotes from global and regional banks, broker/dealers, and exchanges.

ABS, RMBS and CMBS: Valued using cash flow modeling and non-binding broker quotes received from brokers who are familiar with these generally illiquid investments. The cash flow model uses prepayment, default and severity assumptions, benchmark yields and spreads and weighted average lives as inputs. A portion of securities is valued using trader-marked bid side dollar prices and spreads to updated swaps curves from a third party pricing vendor. A small segment is valued from non-binding external sources where unobservable inputs are not readily available. TBAs are valued using the market and income approaches by leading, nationally recognized providers of market data and analytics. When available, recent trades of identical or similar assets are used to price these securities.

Common Stocks: Consists of a non-actively traded stock in National Association of Mutual Insurance Companies (NAMIC), whose price is published by the Securities Valuation Office of the National Association of Insurance Commissioners (NAIC), as well as a delisted security which is valued by an external vendor using unobservable inputs.

Securities Sold, Not Yet Purchased: Valued using the market and income approaches by leading, nationally recognized providers of market data and analytics. When available, recent trades of identical or similar assets are used to price these securities. Securities sold, not yet purchased are included with other liabilities within the consolidated balance sheets.

Other Valuations

Includes private equity and common stock investments presented using equity and cost methods of accounting, policy loans carried at their outstanding principal balance, mortgage loans carried at their outstanding principal amount and cash. Also includes trust preferred debentures and surplus notes carried at their outstanding principal balance.

(in thousands of dollars)

The following summarizes the Company's financial assets and liabilities measured at fair value as of December 31:

2018

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Other Valuations	Balance as of December 31, 2018
Financial assets					
Bonds:					
U.S. government	$ 1,312,482	$ 253,982	$ —	$ —	$ 1,566,464
Municipals	—	5,777,302	2,939	—	5,780,241
Corporates	—	4,673,776	—	—	4,673,776
RMBS	—	1,144,196	2	—	1,144,198
CMBS	—	1,053,955	2,990	—	1,056,945
ABS	—	1,167,221	147,155	—	1,314,376
Common stocks	2,297,955	11,057	1,526	58,420	2,368,958
Cash equivalents	518,646	145,176	—	—	663,822
Short-term investments	88,588	93,433	—	—	182,021
Separate account assets	—	285,614	—	—	285,614
Total recurring basis assets	4,217,671	14,605,712	154,612	58,420	19,036,415
Valued at cost, amortized cost, or using the equity method	—	—	—	2,240,308	2,240,308
Total financial assets	$ 4,217,671	$ 14,605,712	$ 154,612	$ 2,298,728	$ 21,276,723
Financial liabilities					
Debt	$ —	$ 606,920	$ —	$ 206,445	$ 813,365
Derivative liabilities	—	4,068	—	—	4,068
Securities sold, not yet purchased	—	—	—	—	—
Total financial liabilities	$ —	$ 610,988	$ —	$ 206,445	$ 817,433

2017

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Other Valuations	Balance as of December 31, 2017
Financial assets					
Bonds:					
U.S. government	$ 711,233	$ 299,086	$ —	$ —	$ 1,010,319
Municipals	—	5,063,645	17,039	—	5,080,684
Corporates	—	4,974,433	2,483	—	4,976,916
RMBS	—	621,374	116,232	—	737,606
CMBS	—	718,154	9,347	—	727,501
ABS	—	959,201	80,513	—	1,039,714
Common stocks	2,575,481	13,515	2	57,818	2,646,816
Cash equivalents	474,803	—	—	—	474,803
Short-term investments	136,453	20,811	—	—	157,264
Derivative assets	—	—	—	—	—
Separate account assets	—	331,049	—	—	331,049
Total recurring basis assets	3,897,970	13,001,268	225,616	57,818	17,182,672
Valued at cost, amortized cost, or using the equity method	—	—	—	2,102,183	2,102,183
Total financial assets	$ 3,897,970	$ 13,001,268	$ 225,616	$ 2,160,001	$ 19,284,855
Financial liabilities					
Debt	$ —	$ 647,566	$ —	$ 166,439	$ 814,005
Derivative liabilities	—	2,374	—	—	2,374
Securities sold, not yet purchased	—	—	4,415	—	4,415
Total financial liabilities	$ —	$ 649,940	$ 4,415	$ 166,439	$ 820,794

As part of its pricing procedures, the Company obtains quotes from leading providers of pricing data, and the Company's internal pricing policy is to use consistent sources for individual securities based on security type in order to maintain the integrity of its valuation process. These primary quotes are validated on a quarterly basis via comparison to a secondary pricing source, which may include quotes received from a different third party pricing data provider or recent trade activity obtained from reputable online trading sites. Investment managers may be consulted to corroborate prices received from outside sources based on their knowledge of market trends and activity. As necessary, the Company utilizes a pricing service that specializes in difficult-to-value securities to price esoteric or illiquid securities. Material discrepancies between the primary and secondary sources are investigated, reconciled, and updated as warranted. This may involve challenging a price from the primary source if the Company determines the price provided does not meet expectations based on observed market, sector, or security trends and activity.

On an annual basis, the Company reviews quality control measures and data assumptions from its pricing sources to determine if any significant changes have occurred that may indicate issues or concerns regarding the evaluation or market coverage. In addition, an annual analysis is performed on a sample of securities to further validate the inputs, assumptions, and methodologies used by the primary source to price those securities.

During the course of the valuation process, if it is determined the material inputs used to price a security are unobservable, the Company will transfer that security to Level 3.

In 2018, the Company transferred the following securities from Level 2 to Level 3: $9,927 of ABS securities due to a third party pricing service pricing these bonds using unobservable inputs. The Company also transferred $4,125 of ABS securities and $3,347 of CMBS securities from Level 3 to Level 2. In 2018, a third party pricing service began pricing these bonds using observable inputs. Previously, these securities were priced by another pricing vendor using unobservable inputs.

In 2017, the Company transferred the following securities from Level 2 to Level 3: $18,575 of ABS securities due to a third party pricing service pricing these bonds using unobservable inputs and $5,293 of Corporates as a result of an impairment of a matrix priced security where observable inputs were no longer available. The Company also transferred $19,758 of ABS securities from Level 3 to Level 2. In 2017, a third party pricing service began pricing these bonds using observable inputs. Previously, these securities were priced by another pricing vendor using unobservable inputs.

There were no other material transfers in to or out of Level 3 in 2018 or 2017.

(in thousands of dollars)

The following provides a summary of purchases and sales during the years ended December 31, of Level 3 financial assets and liabilities held at fair value on a recurring basis at December 31:

	2018		2017	
	Purchases	Sales	Purchases	Sales
Financial assets				
Bonds:				
Municipals	$ —	$ (14,171)	—	$ (375)
Corporates	—	(5,013)	3,750	(8,988)
RMBS	1,008,575	(1,122,715)	1,883,735	(1,892,351)
CMBS	—	(3,002)	10,321	(973)
ABS	128,189	(67,061)	66,224	(130,732)
Common stocks	—	—	—	—
Total Level 3 financial assets	$ 1,136,764	$ (1,211,962)	$ 1,964,030	$ (2,033,419)
Financial liabilities				
Securities sold, not yet purchased	$ 33,756	$ (38,181)	$ 547,458	$ (583,808)
Total Level 3 financial liabilities	$ 33,756	$ (38,181)	$ 547,458	$ (583,808)

The following table summarizes quantitative information about significant unobservable inputs used to value Level 3 securities as of December 31:

	Fair Value At 12/31/2018	**Valuation Technique**	**Unobservable Input**
Municipals	$ 2,939	Par value	Backed by property tax payments made by the Company
RMBS	2	Cash flow modeling	Spread (Discount Margin)
CMBS	2,990	Cash flow modeling	Spread (Discount Margin)
ABS	147,155	Cash flow modeling	Spread (Discount Margin)
Significant unobservable inputs not available:			
Financial assets			
Bonds	—		
Stocks	1,526		
Financial liabilities			
Securities sold, not yet purchased	—		
Total inputs not available	1,526		
Total Level 3 securities	$ 154,612		

(in thousands of dollars)

	Fair Value At 12/31/2017	Valuation Technique	Unobservable Input
Municipals	$ 13,928	Cash flow modeling	Spread (Discount Margin)
	3,110	Par value	Backed by property tax payments made by the Company
RMBS	2	Cash flow modeling	Spread (Discount Margin)
CMBS	9,347	Cash flow modeling	Spread (Discount Margin)
ABS	80,513	Cash flow modeling	Spread (Discount Margin)
Significant unobservable inputs not available:			
Financial assets			
Bonds	118,716		
Financial liabilities			
Securities sold, not yet purchased	(4,415)		
Total inputs not available	114,301		
Total Level 3 securities	$ 221,201		

Mortgage Loans

The fair value of mortgage loans on real estate is based upon discounted future cash flows using the current rates at which similar loans with comparable maturities would be made to borrowers with similar credit ratings.

Policy Loans

Policy loans represent amounts borrowed from the Company by life insurance policyholders, secured by the cash value of the related policies, and are reported at unpaid principal balance. Policy loans have no stated maturity dates and are an integral part of the related insurance contract. The carrying value of policy loans approximates the fair value. The interest rate for policy loans on current issues was 8% in both 2018 and 2017.

Deferred Annuities and Structured Settlements

Fair values for deferred annuities are based on the cash surrender value of the policies. Fair values for structured settlements are based on the present value of expected payments using current crediting interest rates.

Fair Value

The carrying values and fair values of the Companies' significant financial instruments that are not carried at fair value or are not disclosed on the face of the consolidated balance sheets or elsewhere in the notes at December 31 are as follows:

	2018		2017	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Mortgage loans	$ 715,372	$ 711,046	$ 687,606	$ 700,059
Policy loans	192,534	192,534	196,759	196,759
Financial liabilities				
Deferred annuities	267,010	266,408	269,259	268,335
Structured settlements	47,290	55,661	50,585	59,864

(in thousands of dollars)

b. Common Stocks

The aggregate cost of common stocks considered available for sale at December 31, 2018 and 2017 was $1,769,768 and $1,598,118, respectively. Net unrealized appreciation of common stocks stated at fair value includes gross unrealized gains of $630,870 and $1,008,329 and gross unrealized losses of $90,100 and $17,449 at December 31, 2018 and 2017, respectively. The carrying value of common stocks valued using the cost or equity method at December 31, 2018 and 2017 was $58,420 and $57,818, respectively.

The fair value and unrealized losses, categorized by stocks in loss positions for less than 12 months and stocks in loss positions for more than 12 months, at December 31 are as follows:

	2018							
	Less than 12 Months			12 Months or More			Total	
	Number of Issues	Fair Value	Unrealized Losses	Number of Issues	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Description of Securities:								
Common stocks	748	$594,302	$ (81,342)	313	$ 13,167	$ (8,758)	$607,469	$ (90,100)
Total	748	$594,302	$ (81,342)	313	$ 13,167	$ (8,758)	$607,469	$ (90,100)

	2017							
	Less than 12 Months			12 Months or More			Total	
	Number of Issues	Fair Value	Unrealized Losses	Number of Issues	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Description of Securities:								
Common stocks	223	$116,529	$ (8,514)	354	$ 18,426	$ (8,935)	$134,955	$ (17,449)
Total	223	$116,529	$ (8,514)	354	$ 18,426	$ (8,935)	$134,955	$ (17,449)

The Company believes that declines in fair value related to these stocks are temporary. In determining whether these declines in fair value are temporary, the Company considers severity of impairment, duration of impairment, forecasted market price recovery, and the intent and ability of the Company to hold the investment until the market price has recovered.

During 2018 and 2017, the Company recorded OTTI in its stock portfolio, resulting in a total realized loss of $18,299 and $12,284, respectively.

Proceeds from sales of stock during 2018 and 2017 were $1,252,635 and $1,437,652, respectively. These amounts exclude spin-offs, tax-free exchanges, taxable exchanges, and returns of capital. Gross gains of $299,119 and $333,157 and gross losses of $51,232 and $43,441 were realized on those sales during 2018 and 2017, respectively. The basis of the securities sold was determined using specific identification.

During 2018, the Company made charitable contributions of common stock with a fair value of $14,147, and realized gains on the transactions of $13,699. No such contributions were made during 2017.

The Company's common stock portfolios are primarily invested in large-, mid-, and small-cap stocks which are managed to their respective indices. Further separation of equity securities by geography or industry concentration is not deemed relevant.

(in thousands of dollars)

c. Bonds

The amortized cost and fair value of bonds and short-term investments at December 31 are as follows:

	2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Description of Securities:				
U.S. government	$ 1,643,576	$ 15,342	$ (3,866)	$ 1,655,052
Municipals	5,755,693	64,468	(32,429)	5,787,732
Corporates	4,772,183	44,040	(139,483)	4,676,740
RMBS	1,141,642	11,207	(8,651)	1,144,198
CMBS	1,059,021	7,661	(9,738)	1,056,944
ABS	1,393,729	8,431	(4,805)	1,397,355
Total	$ 15,765,844	$ 151,149	$ (198,972)	$ 15,718,021

	2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Description of Securities:				
U.S. government	$ 1,152,010	$ 1,167	$ (6,403)	$ 1,146,774
Municipals	5,010,659	98,589	(20,085)	5,089,163
Corporates	4,845,631	163,691	(21,103)	4,988,219
RMBS	733,786	7,730	(3,910)	737,606
CMBS	723,148	7,796	(3,443)	727,501
ABS	1,039,390	4,531	(3,180)	1,040,741
Total	$ 13,504,624	$ 283,504	$ (58,124)	$ 13,730,004

The fair value and unrealized losses, categorized by bonds in loss positions for less than 12 months and bonds in loss positions for more than 12 months, at December 31 are as follows:

	2018							
	Less than 12 Months			12 Months or More			Total	
	Number of Issues	Fair Value	Unrealized Losses	Number of Issues	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Description of Securities:								
U.S. government	28	$ 209,637	$ (1,197)	28	$ 124,779	$ (2,669)	$ 334,416	$ (3,866)
Municipals	438	1,377,861	(11,650)	495	1,285,684	(20,779)	2,663,545	(32,429)
Corporates	1,384	2,617,162	(106,079)	319	580,068	(33,404)	3,197,230	(139,483)
RMBS	144	215,975	(2,002)	146	206,580	(6,649)	422,555	(8,651)
CMBS	141	419,490	(6,002)	67	124,297	(3,736)	543,787	(9,738)
ABS	153	471,229	(3,527)	22	85,474	(1,278)	556,703	(4,805)
Total	2,288	$ 5,311,354	$ (130,457)	1,077	$ 2,406,882	$ (68,515)	$ 7,718,236	$ (198,972)

(in thousands of dollars)

	2017							
	Less than 12 Months			12 Months or More			Total	
	Number of Issues	Fair Value	Unrealized Losses	Number of Issues	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Description of Securities:								
U.S. government	62	$ 504,335	$ (2,830)	33	$ 298,270	$ (3,573)	$ 802,605	$ (6,403)
Municipals	447	1,174,384	(7,253)	281	768,520	(12,832)	1,942,904	(20,085)
Corporates	442	1,030,028	(9,335)	169	453,692	(11,768)	1,483,720	(21,103)
RMBS	70	203,701	(1,056)	121	178,785	(2,854)	382,486	(3,910)
CMBS	91	186,070	(1,092)	44	104,530	(2,351)	290,600	(3,443)
ABS	127	534,258	(2,582)	24	62,126	(598)	596,384	(3,180)
Total	1,239	$ 3,632,776	$ (24,148)	672	$ 1,865,923	$ (33,976)	$ 5,498,699	$ (58,124)

The Company classifies certain bond investments as trading securities, and unrealized gains and losses related to these securities are included in net investment income. The fair value of these securities was $36,972 as of December 31, 2018. The change in unrealized gains (losses) recorded in income relating to trading securities held at December 31, 2018 was $(1,812). The Company did not own any trading securities as of December 31, 2017.

If the Company has the intent to sell or will more likely-than-not be required to sell a fixed income security prior to full recovery, the Company writes down the security to its current fair value with the entire write-down recorded as a realized loss in the consolidated statements of comprehensive income. If the Company does not have the intent to sell but the fixed income security is in an unrealized loss position, the Company determines if any of the decline in value is due to a credit-related loss (the present value of the expected future cash flows (PVCF) is less than amortized cost). Other-than-temporary, credit-related impairments are recorded in earnings when the PVCF is less than the amortized cost. Any non-credit-related impairments, such as those related to movement in interest rates, are included with unrealized gains and losses in other comprehensive income. The Company believes that all other unrealized losses related to bonds are temporary.

In determining OTTI, the Company considers severity of impairment, duration of impairment, forecasted market price recovery, and the intent and ability of the Company to hold the investment until the market price recovers or the investment matures to assist in determining if a potential credit loss exists. Additionally, the Company may rely on the details of settlements reached in bankruptcy proceedings or other restructurings to determine ultimate collectability of these investments. The Company does not hold any impaired fixed income securities where part of the impairment was considered credit-related and part of the impairment was non-credit-related.

During 2018 and 2017, the Company recorded total OTTI relating to its bond portfolio of $0 and $2,483, respectively. These amounts represent only credit-related impairments as the Company recognized no impairments due to the intent to sell securities. No portion of the OTTI loss was included in accumulated other comprehensive income.

(in thousands of dollars)

The amortized cost and fair value of bonds and short-term investments at December 31, 2018 are shown below by contractual maturity. Expected maturities may differ from contractual maturities because borrowers may exercise the right to call or prepay obligations with or without penalties. Because most mortgage-backed and asset-backed securities provide for periodic payments throughout their lives, they are listed in a separate category as follows:

	December 31, 2018	
	Amortized Cost	**Fair Value**
Due in one year or less	$ 627,711	$ 628,679
Due after one year through five years	4,153,403	4,136,452
Due after five years through ten years	4,262,472	4,223,813
Due after ten years	3,127,866	3,130,580
Subtotal	12,171,452	12,119,524
Mortgage-backed securities	2,200,663	2,201,142
Asset-backed securities	1,393,729	1,397,355
Total	$ 15,765,844	$ 15,718,021

Proceeds from sales of long-term bonds during 2018 and 2017 were $10,980,278 and $9,384,785 and gross gains of $29,141 and $52,533 and gross losses of $127,344 and $52,736 were realized on those sales during 2018 and 2017, respectively. The basis of the securities sold was determined using specific identification.

At December 31, 2018 and 2017, bonds with a fair value of $76,168 and $56,788, respectively, were on deposit with various regulatory authorities to comply with insurance laws.

d. Other Invested Assets

The Company held $659,125 and $508,861 in limited partnerships accounted for under the cost method and $509,204 and $488,790 in limited partnerships accounted for under the equity method at December 31, 2018 and 2017, respectively. See Note 1(b) for a description of specific accounting practices regarding the cost and equity methods and Note 5 for a description of required future contributions to limited partnerships. The Company also held $69,732 and $0 in non-limited partnership other invested assets at December 31, 2018 and 2017, respectively.

During 2018 and 2017, the Company recorded OTTI in the other invested assets portfolio, resulting in a total realized loss of $7,979 and $8,615, respectively. The other-than-temporarily impaired investments were generally mature partnerships that had completed their initial investment period. Some were in the process of liquidating investment holdings. These partnerships may have experienced losses due to poor performance of a specific investment, poor performance of a particular sector, or unfavorable market conditions in general. As there was no clear indication of full recovery of value of these investments, OTTI losses were realized.

The Company believes that no additional other invested assets in the portfolio are other-than-temporarily impaired. In making this determination, the Company considers severity of impairment, age of the partnership, percentage of the total commitment funded, performance of the underlying investments, sector of the underlying investments, and the intent and ability of the Company to hold the investment until the value has fully recovered.

(in thousands of dollars)

e. Derivative Instruments

In order to mitigate interest rate risk with respect to the Company's investment portfolio and general operations, the Company has entered into certain interest rate derivatives. The Company may also enter into equity options to mitigate market risk within the Company's investment portfolio. All derivative instruments are subject to enforceable master netting agreements and the Company elects to net derivative asset and derivative liability positions with the same counterparty on the consolidated balance sheets. Cash collateral payable (receivable) is recorded net within other assets (liabilities) on the consolidated balance sheets. As a result of an amendment in the Chicago Mercantile Exchange (CME) rulebook in 2017, variation margin payments are now legally characterized as settlements of the derivative position as opposed to collateral and, therefore, are no longer included within cash collateral (received) pledged balances. This amendment also results in the fair value of interest rate swaps being shown net of variation margin in the tables below.

Derivative instruments as of December 31, 2018 and 2017 are as follows:

	2018					
			Balance Sheet		Statement of Comprehensive Income	
Derivatives designated as:	**Notional (Par) Value**	**Purpose**	**Classification**	**Fair Value**	**Classification**	**Amount Realized**
Non-hedging instruments						
Assets:						
Interest rate swaps	$ —	Manage duration	Other assets	$ —	Net investment income	$ —
Liabilities:						
Interest rate swaps	1,420,000	Manage duration	Other liabilities	(4,068)	Net investment income	276
Total open positions	$ 1,420,000			$ (4,068)		$ 276
Closed:						
Interest rate swaps	$ 360,010	Manage duration	N/A		Net investment income	$ 3,714
Equity options	75,675	Hedge credit exposure	N/A		Net investment income	4,527
Total closed positions	$ 435,685					$ 8,241
					Total	$ 8,517

	2017					
			Balance Sheet		Statement of Comprehensive Income	
Derivatives designated as:	**Notional (Par) Value**	**Purpose**	**Classification**	**Fair Value**	**Classification**	**Amount Realized**
Non-hedging instruments						
Assets:						
Interest rate swaps	$ —	Manage duration	Other assets	$ —	Net investment income	$ —
Liabilities:						
Interest rate swaps	1,255,000	Manage duration	Other liabilities	(2,374)	Net investment income	(4,991)
Total open positions	$ 1,255,000			$ (2,374)		$ (4,991)
Closed:						
Interest rate swaps	$ 316,200	Manage duration	N/A		Net investment income	$ 254
Total closed positions	$ 316,200					$ 254
					Total	$ (4,737)

(in thousands of dollars)

The following table provides gross and net amounts for the Company's derivative instruments:

	2018					
					Amounts Not Offset on Balance Sheet	
Derivatives Designated as:	Gross Amount	Counterparty Netting	Cash Collateral (Received) Pledged	Net Amount on Balance Sheet	Securities Collateral (Received) Pledged	Net Amount
Assets	$ 12,180	$ (12,180)	$ —	$ —	$ —	$ —
Liabilities	(14,953)	12,180	—	(2,773)	—	(2,773)
Total	$ (2,773)	$ —	$ —	$ (2,773)	$ —	$ (2,773)

	2017					
					Amounts Not Offset on Balance Sheet	
Derivatives Designated as:	Gross Amount	Counterparty Netting	Cash Collateral (Received) Pledged	Net Amount on Balance Sheet	Securities Collateral (Received) Pledged	Net Amount
Assets	$ 6,685	$ (9,059)	$ (138)	$ (2,512)	$ —	$ (2,512)
Liabilities	(9,059)	9,059	—	—	—	—
Total	$ (2,374)	$ —	$ (138)	$ (2,512)	$ —	$ (2,512)

Collateral pledged as initial margin to the CME is not subject to a master netting agreement and is therefore excluded from collateral pledged (received) in the previous table.

Counterparty credit risk is evaluated closely to ensure that the party or collateral backing the derivative transaction will meet the financial obligations of the contract. For bilateral over-the-counter interest rate swap transactions the amount of counterparty exposure depends on the creditworthiness of and collateral provided by the counterparty. The Company actively monitors and evaluates the financial qualifications of counterparties to its swap agreements and requires these counterparties to provide sufficient collateral security through the execution of a legally enforceable Credit Support Annex (CSA). The CSA requires collateral to be exchanged when predetermined exposure limits are exceeded and permits either party to net collateral transfers due for transactions covered under the agreements. Bonds pledged by the Company as collateral are included in bonds, available-for-sale, on the consolidated balance sheets. Bonds pledged by counterparties to the Company as collateral are not recognized by the Company as assets, as they remain in the custody of the party making the pledge. Cash collateral pledged to (by) the Company is recorded net within other assets (liabilities) on the consolidated balance sheets as previously described. As of December 31, 2018, the only collateral outstanding related to bilateral OTC interest rate swap transactions is $653 in cash that the Company has pledged to counterparties as initial margin. The Company had no bilateral OTC interest rate swap transactions open as of December 31, 2017, and thus had no collateral pledged to or from OTC counterparties.

Substantially all swap contracts were transacted and cleared through the central clearinghouse at the CME, where the CME serves as the counterparty for both parties to the swap contract. Rather than directly posting collateral to/from a traditional counterparty as in a bilateral agreement, the Company posts initial and variation margin per CME's requirements. Initial margin, which may consist of cash and/or securities, protects against "shock" events and is not used to settle market value variation movements. After initial execution of the swap contract, the CME uses a market-standard model to price (mark to market) accepted trades, and that price serves as the basis for variation margin requirements. Similar to the movement of collateral between counterparties in a bilateral agreement, centrally cleared swap contracts require variation margin to be posted (received) by the Company as the market value of the swap contract moves further out of (into) the money. As of December 31, 2018 and 2017, the Company pledged no cash as initial margin but pledged bonds with a fair value of $10,255 and $6,450, respectively, to the CME as initial margin. The Company pledged no cash as variation margin to the CME as of December 31, 2018 or 2017. The CME posted $1,361 and $138 in cash as variation margin to the Company as of December 31, 2018 and 2017, respectively. Cash pledged as variation margin by (to) the Company and bonds pledged as collateral by (to) the Company are handled exactly as those discussed in relation to OTC counterparties in the paragraph above.

(in thousands of dollars)

Counterparty credit exposure by counterparty credit rating as it relates to open derivative positions as of December 31, 2018 and 2017, is as follows:

	2018			
Rating	**Number of Counterparties**	**Notional (Par) Value**	**Credit Exposure**	**Exposure, Net of Collateral**
Centrally cleared	1	$ 1,355,000	$ (2,773)	$ —
A-	1	65,000	(1,295)	—
Total	2	$ 1,420,000	$ (4,068)	$ —

	2017			
Rating	**Number of Counterparties**	**Notional (Par) Value**	**Credit Exposure**	**Exposure, Net of Collateral**
Centrally cleared	1	$ 1,255,000	$ (2,374)	$ —
A-	—	—	—	—
Total	1	$ 1,255,000	$ (2,374)	$ —

f. Net Investment Income

Net investment income for the years ended December 31 is summarized as follows:

	2018	2017
Bonds	$ 480,285	$ 417,012
Common stocks	44,406	50,689
Real estate	52,785	49,265
Mortgage loans	31,865	30,574
Policy loans	14,127	14,611
Limited partnerships and joint ventures	155,554	123,340
Other	(3,817)	2,280
Total gross investment income	775,205	687,771
Change in value of trading securities	(1,812)	—
Change in value of derivatives	8,517	(4,737)
Change in fair value of long-term debt	40,646	(45,711)
Investment expenses	(123,119)	(114,042)
Net investment income	$ 699,437	$ 523,281

g. Mortgage Loans

The minimum and maximum lending rates for commercial mortgage loans issued during 2018 and 2017 ranged from 4.37% to 5.31% and 3.78% to 5.14%, respectively. During 2018 and 2017, the Company did not reduce interest rates on outstanding mortgage loans.

Mortgage loans of the Company are invested primarily in office, retail, and industrial properties and are reported and measured at their outstanding principal amount. Fire and extended coverage insurance is required on all properties. The maximum percentage of any one loan to the value of security at the time of the loan, exclusive of insured or guaranteed or purchase money mortgages did not exceed 67%.

(in thousands of dollars)

Significant concentrations of mortgage loans amounting to $350,347 and $343,488 exist for properties located in the South region at December 31, 2018 and 2017, respectively. In addition, significant concentrations of mortgage loans by state include the following as of December 31:

	2018	2017
Texas	$ 122,185	$ 108,269
California	89,944	75,199
Georgia	71,226	71,805

The Company considers any loan that is one or more days delinquent to be past due. At December 31, 2018 and 2017, the Company had no past due commercial mortgage loans, and there were no recorded investments in impaired loans during both 2018 and 2017. As of December 31, 2018 and 2017, all loans in the portfolio were in good standing, and no loans had been modified or restructured.

A loan is considered to be in good standing if all payments are current. When reviewing loans for impairment and making the determination to increase the valuation allowance or to charge off a loan, the Company individually monitors and analyzes loans and does not utilize portfolio segments or classes for monitoring purposes. The Company considers delinquency or default of payments, the mortgage loan unpaid principal balance as a percent of the fair value of the mortgage loan collateral, present value of expected payments compared to the current carrying value of the mortgage, current rent rolls of the property, financial condition of major tenants, and local economic conditions that would impact individual loans when reviewing potential loan impairment.

If analysis of any of these factors suggests the ability of the borrower to make future payments may be compromised or if the loan is delinquent in its payments by fewer than 90 days, the loan is added to the Company's watchlist. A watchlist loan has developed negative characteristics or trends in the impairment indicators discussed above, but has not yet met the criteria of a non-performing loan. Specific examples of such watchlist indicators may include loss of a major tenant or delinquency of property tax payments. Watchlist loans are monitored closely by the Company for indications of possible default, and an allowance may be established if ultimate collectability of the full principal amount becomes uncertain. If a loan is 90 days or more past due or is in the process of foreclosure, the loan is reclassified as non-performing. Non-performing loans are reserved to an amount equal to the expected potential principal loss and are reviewed in detail to determine whether an impairment or charge-off is necessary. Charge-offs are recorded when principal loss is imminent and the amount is readily determinable.

The Company had $715,372 and $687,606 of loans outstanding as of December 31, 2018 and 2017, respectively, of which $3,031 and $9,724 were on the watchlist. There were no non-performing loans held as of December 31, 2018 and 2017. There were no charge-offs recorded in the mortgage loan portfolio in 2018 and 2017.

The Company did not carry a valuation allowance for credit losses on mortgage loans as of December 31, 2018 and 2017.

Commercial mortgage loans are placed on nonaccrual status after a default notice has been issued and the borrower has failed to cure the defect in a reasonable amount of time. Once a loan reaches nonaccrual status any accrued interest income is derecognized and future accrual of interest is suspended until the loan is made current. If the ultimate collectability of principal, either in whole or in part, is in doubt, any payment received on a nonaccrual loan shall first be applied to reduce principal to the extent necessary to eliminate such doubt. There were no loans in nonaccrual status at December 31, 2018 and 2017, and no loans were restructured during 2018 or 2017.

(in thousands of dollars)

h. Fair Value Option (FVO) of Long-Term Debt

The following table presents information for a liability which is accounted for under the FVO at December 31, 2018 and 2017. This liability consists of the balance of the 30-year fixed rate FHLBC debt which was measured at fair value upon receipt of the advance (see Note 11).

Liabilities:	**2018**	**2017**
Contractual principal balance	$ 500,000	$ 500,000
Difference between estimated fair value and contractual principal balance	106,920	147,566
Carrying value at estimated fair value	$ 606,920	$ 647,566

Changes in fair value of this liability of $(40,646) and $45,711 are recognized as an increase and a decrease in net investment income for the years ended December 31, 2018 and 2017, respectively.

Fair value for the FHLBC advance is based upon a discounted cash flow analysis using observable market inputs. Electing the fair value option of this liability better reflects the economic position of the debt instrument due to the prepayment option of the FHLBC advance.

The Company has not elected the FVO for any other debt instrument.

4. Deferred Policy Acquisition Costs

DAC and the related amortization charged to income were as follows:

	2018	**2017**
Life		
Balance, beginning of year	$ 344,465	$ 326,527
Costs deferred during year	28,983	25,726
Amortization related to operations during year	(19,787)	(13,996)
Net adjustment due to assumption revisions	3,223	18,064
Amounts related to change in fair value adjustment of available-for-sale bonds	40,328	(11,856)
Balance, end of year	397,212	344,465
Property & Casualty		
Balance, beginning of year	452,679	436,952
Costs deferred during year	1,238,390	1,173,655
Amortization related to operations during year	(1,182,650)	(1,157,928)
Balance, end of year	508,419	452,679
Other		
Balance, end of year	—	9
Total DAC	$ 905,631	$ 797,153

5. Commitments and Contingencies

The Companies have various leases for property and equipment used in the normal course of business. These lease commitments are summarized in Note 1(n).

The Companies are contingently liable for cessions to reinsurers to the extent that any reinsurer might be unable to meet its obligations assumed under the various reinsurance contracts. Where contracts permit, the Companies secure reinsurance recoverables with various forms of collateral, including irrevocable letters of credit, secured trusts, and funds held accounts.

The Company is liable for losses that arise from assumed reinsurance agreements and has pledged collateral in the form of letters of credit and funds held accounts totaling $40,904 and $41,741 at December 31, 2018 and 2017, respectively.

The Company has structured settlements for which the claimant is the payee, but for which the Company is contingently liable. The carrying values of all such structured settlements purchased from nonaffiliated life insurers at December 31, 2018 and 2017 were $51,690 and $56,794, respectively.

The Company enters into contractual agreements that require capital contributions to limited partnerships. These contributions are recorded on the consolidated balance sheets as other invested assets. Capital is typically contributed to the partnerships over multiple years. At any time, the Company will have commitments to the partnerships that have not yet been funded. As of December 31, 2018 and 2017, the Company was obligated to contribute $867,820 and $638,399, respectively, in additional capital to various limited partnerships. These contributions are callable under the commitments to the partnerships over the lives of the partnerships.

The Companies are at times involved in lawsuits which are related to operations. In most cases, such lawsuits involve claims under insurance policies and other contracts of the Companies. Such lawsuits, either individually or in the aggregate, are not expected to have a material effect on the Companies' consolidated financial statements.

The Companies are liable for mandatory assessments that are levied by the property & casualty and life & health guaranty fund associations of states in which the Companies are licensed. These assessments are to cover losses to policyholders of insolvent or rehabilitated insurance companies. Guaranty fund assessment liabilities, as of December 31, 2018 and 2017, were $21,238 and $25,310, respectively. Corresponding assets related to future premium tax credits have also been recorded and were $13,846 and $15,323 as of December 31, 2018 and 2017, respectively. Such estimates are subject to change as the associations determine more precisely the losses that have occurred and how such losses will be allocated to insurance companies.

(in thousands of dollars)

6. Income Taxes

The components of the net deferred tax assets (liabilities) at December 31, 2018 and 2017, respectively, are as follows:

	2018	2017
Deferred tax assets		
Life reserves	$ 54,221	$ 58,179
Unearned premium	120,634	84,197
Reserve discounting, net of salvage and subrogation	54,016	30,125
Deferred compensation	240,655	232,171
Policyholder dividends	1,044	709
Fair value option of long-term debt	24,029	33,465
Tax credit carryforward	63,629	—
Net operating loss carryforward	96,008	24,531
Total deferred tax assets	654,236	463,377
Deferred tax liabilities		
Investments	(143,937)	(299,936)
Deferred policy acquisition costs	(52,421)	(51,361)
Depreciation basis differences	(130,923)	(109,631)
Intangible assets	(96,720)	(31,524)
Valuation allowance	(12,609)	(4,937)
Pension accrual	(55,093)	(19,704)
Other	(18,436)	(10,348)
Total deferred tax liabilities	(510,139)	(527,441)
Net deferred tax assets (liabilities)	$ 144,097	$ (64,064)

As of December 31, 2018, the Company has net operating loss carryforwards of $396,580 which will expire at various times through 2038.

On December 22, 2017, the Tax Cuts and Jobs Act (the Act) was enacted into law. As a result, in 2017 the Company recognized a tax benefit of $37,369 due to the remeasurement of deferred tax assets and liabilities at lower enacted tax rates.

(in thousands of dollars)

The effective tax rate used to determine the provision for current and deferred tax expense differs from the expected statutory rate as the result of permanent and other differences between pre-tax income and taxable income determined under existing tax regulations. The more significant differences, their effect on the statutory tax rate, and the resulting effective tax rates are summarized as follows:

	2018	2017
Federal statutory tax rate	21.0%	35.0 %
Tax-exempt income, net of proration	(4.0)	(15.2)
Dividend received deduction	(1.6)	(8.3)
State tax expense (net of federal tax)	1.1	(0.1)
Change in prior years' tax - return to provision	(0.3)	1.2
Change in enacted rates on deferred taxes	(7.8)	(25.0)
Reclassification from other comprehensive income	(0.7)	7.2
Other	0.6	0.8
Effective tax rate	8.3%	(4.4)%

The guidance for accounting for uncertainty in income taxes prescribes a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. Interest and penalties on tax uncertainties are classified as a federal tax expense. The total amount of interest accrued was $457 at both December 31, 2018 and 2017. The Company does not expect to have a significant change in unrecognized tax benefits in the next twelve months.

The examinations of the Company’s consolidated federal income tax returns for the years 2014 and prior are closed, and the years 2015 through 2018 remain open under the Internal Revenue Service (IRS) statute of limitations. AFMICSI and its subsidiaries are currently under federal audit for tax year 2015.

7. Goodwill and Intangible Assets

The Company’s business acquisitions resulted in the identification of certain intangible assets and goodwill. Intangible assets with finite lives are amortized over their estimated useful lives of one to sixteen years. Finite-lived intangible assets have a weighted average remaining useful life of approximately five and six years at December 31, 2018 and 2017, respectively. Intangible assets with indefinite lives are considered to have an infinite life and will not be amortized, but are evaluated at least annually for impairment. The Company completes an annual test for goodwill impairment during the fourth quarter based on the results of operations through September and future profit and growth projections and concluded that neither goodwill nor intangible assets were impaired in 2018 or 2017.

Goodwill acquired in 2018 was $233,604 and relates entirely to the acquisition of MSAG. Goodwill acquired in 2017 was $108,165. Of this amount, $93,278 related to the acquisition of NI. See Note 2 for further information on the Company's business combinations.

(in thousands of dollars)

The following presents a summary of the Company's goodwill and unamortized intangible assets at December 31:

	2018		2017	
	Gross Balance	**Accumulated Amortization**	**Gross Balance**	**Accumulated Amortization**
Total goodwill	$ 561,878	$ —	$ 329,792	$ —
Trade name and trademarks	38,500	16,016	25,900	12,950
Partner relationships	97,100	31,906	97,100	21,735
Broker relationships	21,000	97	—	—
Referral relationships	11,100	10,195	11,100	9,799
Software	36,260	25,185	33,470	23,000
Renewal rights	83,700	53,059	56,500	45,530
Value of business acquired	147,400	12,283	—	—
Other	7,786	2,632	2,876	—
Total finite life intangible assets	442,846	151,373	226,946	113,014
State insurance licenses	53,590	—	28,310	—
Total indefinite life intangible assets	53,590	—	28,310	—
Total goodwill and intangible assets	$ 1,058,314	$ 151,373	$ 585,048	$ 113,014

The Company recognized $38,359 and $22,762 of amortization expense related to intangible assets within other expenses in the consolidated statements of comprehensive income for the years ended December 31, 2018 and 2017, respectively.

The estimated amortization expense related to intangible assets with a finite life for each of the next five years is as follows:

2019	$ 100,678
2020	85,681
2021	23,227
2022	21,337
2023	16,435
Total	$ 247,358

8. Employee Benefit Plans

a. AFMICSI Employee Pension and Postretirement Benefits

AFMICSI has a non-contributory qualified pension plan (herein referred to as the Plan) covering employees of AFMICSI only. For AFMICSI employees hired before January 1, 2009, and Sales District Leaders hired before January 1, 2010, the benefits are based on years of credited service and highest average compensation (as defined in the Plan). For employees hired on or after January 1, 2009, and Sales District Leaders hired on or after January 1, 2010, benefits are determined under a cash balance formula (as defined in the Plan). The Company's funding policy is to annually contribute an amount equal to the minimum required contribution per IRS rules and regulations, plus additional amounts at the Company's discretion. Benefit restrictions required under the Pension Protection Act of 2006 do not apply in 2018 or 2017 given the funded status of the Plan.

(in thousands of dollars)

AFMICSI provides certain health care benefits to substantially all AFMICSI employees and contributes toward eligible employees' postretirement health care using a fixed amount for each year of eligible service. Certain employees may also receive health care benefits upon retirement via conversion of unused sick days earned prior to 2008. In addition, AFMICSI provides most AFMICSI employees with a life insurance benefit, for which the Companies absorb substantially all of the cost. The Companies' portions of the costs of these programs are unfunded. The Companies sponsor no other significant postretirement benefit plans and use a measurement date of December 31 for valuing pension and other postretirement benefit plans.

The following table reflects components of amounts recognized in the Company's consolidated balance sheets and the accumulated benefit obligation at December 31:

	Pension Benefits					
	Overfunded		Underfunded		Other Benefits	
	2018	2017	2018	2017	2018	2017
Projected benefit obligation	$ 1,128,525	$ —	$ 41,420	$ 1,283,358	$ 64,626	$ 66,498
Fair value of plan assets	1,364,719	—	—	1,013,365	—	—
Funded status	$ 236,194	$ —	$ (41,420)	$ (269,993)	$ (64,626)	$ (66,498)
Assets:						
Prepaid benefit costs	$ 492,322	$ —	$ —	$ —	$ —	$ —
Recognized in accumulated other comprehensive income	(256,128)	—	—	—	—	—
Net balance sheet asset	$ 236,194	$ —	$ —	$ —	$ —	$ —
Liabilities:						
Accrued (prepaid) benefit costs	$ —	$ —	$ 27,634	$ (18,333)	$ 75,933	$ 74,231
Recognized in accumulated other comprehensive income	—	—	13,786	288,326	(11,307)	(7,733)
Net balance sheet liability	$ —	$ —	$ 41,420	$ 269,993	$ 64,626	$ 66,498
Accumulated benefit obligation	$ 970,801	$ —	$ 33,116	$ 1,079,614	$ 64,626	$ 66,498

The following table reflects amounts in accumulated other comprehensive income (loss) that have not yet been recognized as components of net periodic benefit costs at December 31:

	Pension Benefits					
	Overfunded		Underfunded		Other Benefits	
	2018	2017	2018	2017	2018	2017
Net transition asset or obligation	$ —	$ —	$ —	$ —	$ —	$ —
Net prior service cost or credit	(27,808)	—	(179)	(34,815)	(14,419)	(15,750)
Net unrecognized gains and losses	283,936	—	13,965	323,141	3,112	8,017
Total	$ 256,128	$ —	$ 13,786	$ 288,326	$ (11,307)	$ (7,733)

(in thousands of dollars)

The following table reflects components of amounts recognized in the Company's consolidated statements of comprehensive income at December 31:

	Pension Benefits					
	Overfunded		Underfunded		Other Benefits	
	2018	2017	2018	2017	2018	2017
Net periodic benefit cost	$ 52,305	$ —	$ 4,039	$ 59,266	$ 4,500	$ 4,212
Employer contribution	500,000	—	2,553	85,344	2,985	2,348
Benefits paid	(79,255)	—	(2,553)	(72,765)	(2,985)	(2,348)

The Company recognized additional pension expenses in connection with settlement accounting, which resulted from lump sum distributions exceeding service and interest cost during the year, of $128 and $857 for 2018 and 2017, respectively.

The following table presents amounts recognized in other comprehensive income during 2018:

	Pension Benefits		
	Overfunded	Underfunded	Other Benefits
Actuarial gain (loss)	$ (6,154)	$ 3,674	$ 4,653
Less: Amortization of actuarial gain (loss)	26,011	1,581	252
Prior service cost	—	—	—
Less: Amortization of prior service cost	(6,755)	(73)	(1,331)
Actuarial gain (loss) recognized due to settlement	—	—	—
Less: Amortization of actuarial gain (loss) due to settlement	—	128	—
Prior service cost recognized due to settlement	—	—	—
Less: Amortization of prior service cost due to settlement	—	—	—
Net recognized in other comprehensive income	$ 13,102	$ 5,310	$ 3,574

The following table represents estimated amounts to be amortized in next year's net periodic benefit cost from accumulated other comprehensive income:

	Pension Benefits		
	Overfunded	Underfunded	Other Benefits
Net actuarial (gain)/loss	$ 8,927	$ 962	$ 100
Net prior service cost	(6,754)	(73)	(1,331)
Net transition asset or obligation	—	—	—
Total	$ 2,173	$ 889	$ (1,231)

(in thousands of dollars)

The weighted-average assumptions used in determining projected benefit obligations and net periodic benefit cost as of December 31 are as follows:

	2018	2017
Projected benefit obligations:		
Discount rate		
Overfunded pension plan	4.20%	n/a
Underfunded pension plans	4.09	3.54%
Other benefit plans	4.17	3.50
Rate of compensation increase		
Overfunded pension plan	3.50	n/a
Underfunded pension plans	3.50	3.50
Net periodic benefit cost:		
Discount rate		
Overfunded pension plan	3.55	n/a
Underfunded pension plans	3.42	3.99
Other benefit plans	3.49	3.98
Expected return on plan assets		
Overfunded pension plan	6.25	n/a
Underfunded pension plans	n/a	6.25
Rate of compensation increase		
Overfunded pension plan	3.50	n/a
Underfunded pension plans	3.50	3.50

Annual rates of increase in the per capita costs of covered health care benefits were assumed to be 8.20% and 7.25% (Pre-65) and 8.20% and 7.50% (Post-65) for 2018 and 2017, respectively. Rates will gradually decrease to 4.50% by 2027.

The expected rate of return on plan assets is based upon an analysis of historical returns and long-term capital market assumptions for each asset class. The expected returns by asset class contemplate a risk free interest rate as of the measurement date and then add a risk premium. The risk premium is a range of percentages and is based upon factors such as expected reinvestment returns and asset manager performance. Finally, an underlying inflation assumption is incorporated to determine the overall expected long-term rate of return assumption.

The target allocation, asset allocation, and fair value of plan assets for the Company's pension plan at the end of 2018 and 2017, by asset category, are as follows:

	Target Allocation		Percentage of Plan Assets, Year End		Fair Value of Plan Assets, Year End	
Asset Category	**2018**	**2017**	**2018**	**2017**	**2018**	**2017**
Equity	40%	55%	40%	59%	$ 542,692	$ 599,426
Debt	50	40	44	38	605,545	381,870
Private Equity	10	5	2	3	22,674	25,024
Cash Equivalents	—	—	14	—	189,317	3,327
Total	100%	100%	100%	100%	$ 1,360,228	$ 1,009,647

The overall investment objective of the Plan is to maximize the risk adjusted return on assets over a long-term period, while ensuring the Plan is able to meet current and future obligations to plan participants. The primary considerations in developing target asset allocations are the Plan's overall investment objective, the investment objectives for the various assets, the necessary level of diversification, and maintaining an acceptable level of risk. The existing allocations are within the Company's tolerance for variation from target allocation.

The Company has no significant concentrations of risk within Plan assets.

Plan assets at fair value are categorized in the same manner as Company assets, based on the reliability of inputs to the valuation techniques as described in Note 1(c).

Below is a summary of significant valuation techniques specific to Plan assets:

Level 1 Measurements

Bonds: *U.S. Government*: Comprised of U.S. Treasuries valued based on unadjusted quoted prices for identical assets in active markets.

Equity Securities: *Common Stocks*: Comprised of actively traded, exchange listed U.S. and international equity securities. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Plan can access.

Equity Securities: *Registered Investment Companies*: Comprised of an actively traded, U.S. Treasury bond exchange-traded fund (ETF) with valuations based on unadjusted quoted prices for identical assets in markets that are generally active.

Cash Equivalents: Comprised of actively traded money market funds that have daily quoted net asset values for identical assets that the Plan can access.

Level 2 Measurements

Bonds: *Corporates, Municipals, and Foreign*: Valued using the market and income approaches based on inputs including quoted prices for identical or similar assets in markets that are not active, benchmark yield curves, bid/ask spreads, credit quality, and projected cash flows.

Equity Securities: *Registered Investment Companies and Common/Collective Trusts:* Comprised of non-actively traded U.S. and international funds priced by the fund manager using observable inputs primarily consisting of quoted prices of the underlying investments.

Level 3 Measurements

Limited Partnerships: Valued using capital account valuations as reported by the various limited partnerships, which approximate fair value.

(in thousands of dollars)

The following summarizes the Plan's financial assets measured at fair value as of December 31:

2018

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2018
Financial assets				
Bonds, available-for-sale:				
U.S. government	$ 6,191	$ —	$ —	$ 6,191
Corporates	—	174,910	—	174,910
Foreign bonds	—	41,932	—	41,932
Equity securities				
Common stocks, available-for-sale	356,036	—	—	356,036
Registered investment companies	308,642	153,171	—	461,813
Common/collective trusts	—	107,355		107,355
Cash equivalents	189,317	—	—	189,317
Limited partnerships*	—	—	22,674	22,674
Total recurring basis financial assets	$ 860,186	$ 477,368	$ 22,674	$ 1,360,228

2017

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2017
Financial assets				
Bonds, available-for-sale:				
U.S. government	$ 62,054	$ —	$ —	$ 62,054
Corporates	—	204,768	—	204,768
Municipals	—	865	—	865
Foreign bonds	—	43,677	—	43,677
Equity securities				
Common stocks, available-for-sale	275,434	—	—	275,434
Registered investment companies	—	215,666	—	215,666
Common/collective trusts	—	178,832	—	178,832
Cash equivalents	3,327	—	—	3,327
Limited partnerships*	—	—	25,024	25,024
Total recurring basis financial assets	$ 340,815	$ 643,808	$ 25,024	$ 1,009,647

* Limited partnerships were valued using 9/30 capital account valuations provided by the various limited partnerships, adjusted for any capital calls made and distributions received between 9/30 and 12/31.

All transfers into or out of a particular level are recognized as of the beginning of the reporting period. There were no transfers into or out of Level 1, 2, or 3 during 2018 or 2017.

(in thousands of dollars)

The table below sets forth a summary of changes in the fair value of the Plan's Level 3 assets for the year ended December 31, 2018 and 2017:

	Limited Partnerships	
	2018	**2017**
Balance, beginning of year*	$ 25,024	$ 30,479
Purchases, sales, issuance and settlements, net	(2,350)	(5,455)
Balance, end of year*	$ 22,674	$ 25,024

* Limited partnerships were valued using 9/30 capital account valuations provided by the various limited partnerships, adjusted for any capital calls made and distributions received between 9/30 and 12/31.

Expected Cash Flows

Information about the expected cash flows for the Plans follows:

	Pension Benefits		
	Overfunded	**Underfunded**	**Other Benefits**
Expected employer contributions			
2019	$ —	$ 3,312	$ 4,631

The Company made a contribution of $500,000 during 2018 which resulted in the AFMICSI qualified pension plan being overfunded at December 31, 2018. As a result, employer contributions are not expected for the next several years.

	Pension Benefits		
	Overfunded	**Underfunded**	**Other Benefits**
Expected benefit payments			
2019	$ 85,063	$ 3,312	$ 4,631
2020	86,310	3,416	4,541
2021	88,112	3,692	4,659
2022	90,556	4,171	4,918
2023	92,915	4,099	5,145
2024 - 2028	472,645	15,388	27,681

b. NGM Pension and Postretirement Benefits

NGM Insurance Company (NGM), a wholly-owned subsidiary of MSAG, sponsors a non-contributory defined benefit pension plan which provides benefits to substantially all employees of MSAG based upon compensation and length of service. Contributions to the plan are at least equal to the Employee Retirement Income Security Act (ERISA) minimum funding requirements.

NGM provides certain healthcare and life insurance benefits for retired NGM employees. Substantially all NGM employees become eligible for those benefits if they reach age 55, with 15 years of company service. Plan benefits terminate at age 65. NGM uses a December 31 measurement date for its pension and post-retirement benefit plans. NGM's portion of the costs of these programs is unfunded.

(in thousands of dollars)

The following table reflects components of amounts recognized in the Company's consolidated balance sheets and the accumulated benefit obligation at December 31, 2018:

	Pension Benefits		Other Benefits
	Overfunded	**Underfunded**	
Projected benefit obligation	$ 133,687	$ 2,317	$ 6,556
Fair value of plan assets	140,270	—	—
Funded status	$ 6,583	$ (2,317)	$ (6,556)
Assets:			
Prepaid benefit costs	$ 15,374	$ —	$ —
Recognized in accumulated other comprehensive income	(8,791)	—	—
Net balance sheet asset	$ 6,583	$ —	$ —
Liabilities:			
Accrued benefit costs	$ —	$ 2,314	$ 9,957
Recognized in accumulated other comprehensive income	—	3	(3,401)
Net balance sheet liability	$ —	$ 2,317	$ 6,556
Accumulated benefit obligation	$ 133,687	$ 2,317	$ 6,556

The following table reflects amounts in accumulated other comprehensive income (loss) that have not yet been recognized as components of net periodic benefit costs at December 31, 2018:

	Pension Benefits		Other Benefits
	Overfunded	**Underfunded**	
Net transition asset or obligation	$ —	$ —	$ —
Net prior service cost or credit	—	—	—
Net unrecognized gains and losses	8,791	3	(3,401)
Total	$ 8,791	$ 3	$ (3,401)

The following table reflects components of amounts recognized in the Company's consolidated statements of comprehensive income for the period from merger execution (October 31, 2018 - see Note 2) to December 31, 2018:

	Pension Benefits		Other Benefits
	Overfunded	**Underfunded**	
Net periodic benefit cost	$ 551	$ 16	$ 136
Employer contribution	15,000	1	102
Benefits paid	1,509	1	102

(in thousands of dollars)

The following table presents amounts recognized in other comprehensive income during 2018:

	Pension Benefits		
	Overfunded	Underfunded	Other Benefits
Actuarial gain (loss)	$ (8,791)	$ (3)	$ 3,401
Net recognized in other comprehensive income	$ (8,791)	$ (3)	$ 3,401

The following table represents estimated amounts to be amortized in next year's net periodic benefit cost from accumulated other comprehensive income:

	Pension Benefits		
	Overfunded	Underfunded	Other Benefits
Net actuarial (gain)/loss	$ —	$ —	$ (279)
Net prior service cost	—	—	—
Net transition asset or obligation	—	—	—
Total	$ —	$ —	$ (279)

The weighted-average actuarial assumptions used in determining the projected benefit obligations and net periodic benefit cost as of December 31, 2018, are as follows:

Projected benefit obligations:	
Discount rate	
Overfunded pension plan	4.15%
Underfunded pension plans	4.10
Other benefit plans	4.00
Rate of compensation increase	
Overfunded pension plan	3.75
Underfunded pension plans	n/a
Net periodic benefit cost:	
Discount rate	
Overfunded pension plan	4.35
Underfunded pension plans	4.15
Other benefit plans	4.30
Expected return on plan assets	
Overfunded pension plan	6.50
Underfunded pension plans	n/a
Rate of compensation increase	
Overfunded pension plan	3.75
Underfunded pension plans	3.75

Annual rates of increase in the per capita costs of covered health care benefits were assumed to be 8.20% for 2018. Rates will gradually decrease to 4.50% by 2027.

The expected rate of return on plan assets is based upon an analysis of historical returns and long-term capital market assumptions for each asset class. The expected returns by asset class contemplate a risk free interest rate as of the measurement date and then add a risk premium. The risk premium is a range of percentages and is based upon factors such as expected reinvestment returns and asset manager performance. Finally, an underlying inflation assumption is incorporated to determine the overall expected long-term rate of return assumption.

(in thousands of dollars)

The target allocation, asset allocation, and fair value of plan assets for the NGM's pension plan at the end of 2018, by asset category, are as follows:

Asset Category	Target Allocation	Percentage of Plan Assets, Year End	Fair Value of Plan Assets, Year End
Equity	49%	49%	$ 69,184
Debt	41	41	56,853
Other	10	10	14,233
Total	100%	100%	$ 140,270

The overall investment objective of the Plan is to maximize the risk adjusted return on assets over a long-term period, while ensuring the Plan is able to meet current and future obligations to plan participants. The primary considerations in developing target asset allocations are the Plan's overall investment objective, the investment objectives for the various assets, the necessary level of diversification, and maintaining an acceptable level of risk. The existing allocations are within the Company's tolerance for variation from target allocation.

The Company has no significant concentrations of risk within Plan assets.

Plan assets at fair value are categorized in the same manner as Company assets, based on the reliability of inputs to the valuation techniques as described in Note 1(c).

Below is a summary of significant valuation techniques specific to Plan assets:

Level 1 Measurements

Equity Mutual Funds: Comprised of actively traded, exchange listed mutual funds that have daily quoted net asset values for identical assets in active markets that the Plan can access.

Fixed Income Mutual Funds: Comprised of actively traded, exchange listed mutual funds that have daily quoted net asset values for identical assets in active markets that the Plan can access.

Cash Equivalents: Comprised of actively traded money market funds that have daily quoted net asset values for identical assets that the Plan can access.

Other Valuations

Includes common collective trust investments that are valued using the net asset value (NAV) as a practical expedient for fair value.

(in thousands of dollars)

The following summarizes the Plan's financial assets measured at fair value as of December 31:

2018				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2018
Financial assets				
Equity mutual funds	$ 69,184	$ —	$ —	$ 69,184
Fixed income mutual funds	52,755	—	—	52,755
Cash equivalents	4	—	—	4
Total assets in the fair value hierarchy	121,943	—	—	121,943
Investments measured at NAV (a)	—	—	—	18,327
Total recurring basis financial assets	$ 121,943	$ —	$ —	$ 140,270

(a) In accordance with GAAP, certain investments that were measured at NAV per share (or its equivalent) have not been classified in the fair value hierarchy.

The Plan realizes transfers between levels of the fair value hierarchy at the end of the reporting period. There were no transfers into or out of Level 1, 2, or 3 during 2018.

Expected Cash Flows

Information about the expected cash flows for the Plans follows:

	Pension Benefits		Other Benefits
	Overfunded	Underfunded	
Expected employer contributions			
2019	$ —	$ 2,273	$ 596

	Pension Benefits		Other Benefits
	Overfunded	Underfunded	
Expected benefit payments			
2019	$ 8,585	$ 2,273	$ 596
2020	9,356	4	637
2021	10,987	4	603
2022	11,184	4	559
2023	11,618	4	529
2024 - 2028	61,742	17	2,579

c. Other Pension and Postretirement Benefits

Grain Dealers Mutual Insurance Company (GDMIC), an affiliate of NGM, sponsors a non-contributory defined benefit pension plan (the GDMIC plan) covering substantially all GDMIC employees through 2010 who meet certain age and length-of-service requirements. Funding of the GDMIC Plan is based on actuarially recommended contributions. On April 2, 2003, the GDMIC Plan was amended to freeze benefit accruals effective May 31, 2003, and accordingly, benefits will not increase due to service or compensation levels after this date.

(in thousands of dollars)

Austin Mutual Insurance Company (AMIC), an affiliate of NGM, sponsors a non-contributory defined benefit pension plan (the AMIC plan) covering all full-time AMIC employees who have completed one year of qualifying service. During 2009, AMIC froze the defined benefit plan for all full-time AMIC employees. Effective May 15, 2009, no additional employees will become eligible to participate in the defined benefit plan, and no additional accruals will be granted. AMIC's funding policy is to contribute annually the maximum amount that can be deducted for federal income tax purposes. AMIC made no contribution for 2018.

GDMIC sponsored a defined benefit medical plan for substantially all of GDMIC employees. This plan was terminated at December 31, 2010. Participating active GDMIC employees were hired by NGM on January 1, 2011, and became participants in NGM's medical plan, along with retired GDMIC employees.

The following table reflects components of amounts recognized in the Company's consolidated balance sheets and the accumulated benefit obligation at December 31, 2018:

	Pension Benefits	
	GDMIC	AMIC
Projected benefit obligation	$ 18,655	$ 25,486
Fair value of plan assets	16,217	17,584
Funded status	$ (2,438)	$ (7,902)
Liabilities:		
Accrued benefit costs	1,925	6,924
Recognized in accumulated other comprehensive income	513	978
Net balance sheet liability	$ 2,438	$ 7,902
Accumulated benefit obligation	$ 18,655	$ 25,486

The following table reflects amounts in accumulated other comprehensive income (loss) that have not yet been recognized as components of net periodic benefit costs at December 31, 2018:

	Pension Benefits	
	GDMIC	AMIC
Net transition asset or obligation	$ —	$ —
Net prior service cost or credit	—	—
Net unrecognized gains and losses	513	978
Total	$ 513	$ 978

The following table reflects components of amounts recognized in the Company's consolidated statements of comprehensive income for the period from merger execution (October 31, 2018 - see Note 2) to December 31, 2018:

	Pension Benefits	
	GDMIC	AMIC
Net periodic cost	$ (18)	$ 37
Employer contribution	—	89
Benefits paid	267	243

(in thousands of dollars)

The following table presents amounts recognized in other comprehensive income during 2018:

	Pension Benefits	
	GDMIC	AMIC
Actuarial gain (loss)	$ 513	$ 978
Net recognized in other comprehensive income	$ 513	$ 978

There are no estimated amounts to be amortized in next year's net periodic pension cost from accumulated other comprehensive income for either GDMIC or AMIC.

The weighted-average actuarial assumptions used in determining the projected benefit obligations and net periodic benefit cost as of December 31, 2018, are as follows:

Projected benefit obligations:	
Discount rate	
GDMIC	4.05%
AMIC	4.20
Net periodic benefit cost:	
Discount rate	
GDMIC	4.30
AMIC	4.45
Expected rate of return	
GDMIC	5.50
AMIC	5.00

The expected rate of return on plan assets is based upon an analysis of historical returns and long-term capital market assumptions for each asset class. The expected returns by asset class contemplate a risk free interest rate as of the measurement date and then add a risk premium. The risk premium is a range of percentages and is based upon factors such as expected reinvestment returns and asset manager performance. Finally, an underlying inflation assumption is incorporated to determine the overall expected long-term rate of return assumption.

The target allocation, asset allocation, and fair value of plan assets for the GDMIC's and AMIC's pension plans at the end of 2018, by asset category, are as follows:

GDMIC Asset Category	Target Allocation	Percentage of Plan Assets, Year End	Fair Value of Plan Assets, Year End
Equity	26%	26%	$ 4,254
Debt	58	58	9,428
Other	16	16	2,535
Total	100%	100%	$ 16,217

(in thousands of dollars)

AMIC Asset Category	Target Allocation	Percentage of Plan Assets, Year End	Fair Value of Plan Assets, Year End
Equity	32%	31%	$ 5,495
Debt	65	65	11,333
Other	3	4	756
Total	100%	100%	$ 17,584

The overall investment objective of the Plan is to maximize the risk adjusted return on assets over a long-term period, while ensuring the Plan is able to meet current and future obligations to plan participants. The primary considerations in developing target asset allocations are the Plan's overall investment objective, the investment objectives for the various assets, the necessary level of diversification, and maintaining an acceptable level of risk. The existing allocations are within the Company's tolerance for variation from target allocation.

The Company has no significant concentrations of risk within Plan assets.

Plan assets at fair value are categorized in the same manner as Company assets, based on the reliability of inputs to the valuation techniques as described in Note 1(c).

Below is a summary of significant valuation techniques specific to Plan assets:

Level 1 Measurements

Equity Mutual Funds: Comprised of actively traded, exchange listed mutual funds that have daily quoted net asset values for identical assets in active markets that the Plan can access.

Fixed Income Mutual Funds: Comprised of actively traded, exchange listed mutual funds that have daily quoted net asset values for identical assets in active markets that the Plan can access.

Other Valuations

Includes alternative fund investments and pooled separate accounts that are valued at the net asset value (NAV) as a practical expedient for fair value.

(in thousands of dollars)

The following summarizes the GDMIC Plan's financial assets measured at fair value as of December 31:

2018				
GDMIC	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of December 31, 2018
Financial assets				
Equity mutual funds	$ 4,254	$ —	$ —	$ 4,254
Fixed income mutual funds	9,428	—	—	9,428
Total assets in the fair value hierarchy	13,682	—	—	13,682
Investments measured at NAV (a)	—	—	—	2,535
Total recurring basis financial assets	$ 13,682	$ —	$ —	$ 16,217

(a) In accordance with GAAP, certain investments that were measured at NAV per share (or its equivalent) have not been classified in the fair value hierarchy.

As of December 31, 2018, 100 percent of AMIC's plan assets with a fair value of $17,584 were measured using the NAV practical expedient and, therefore have not been classified in the fair value hierarchy in accordance with GAAP.

The Plan realizes transfers between levels of the fair value hierarchy at the end of the reporting period. There were no transfers into or out of Level 1, 2, or 3 during 2018.

Expected Cash Flows
Information about the expected cash flows for the Plans follows:

	Pension Benefits	
	GDMIC	**AMIC**
Expected employer contributions		
2019	$ —	$ 525

	Pension Benefits	
	GDMIC	**AMIC**
Expected benefit payments		
2019	$ 1,612	$ 1,535
2020	1,590	1,573
2021	1,552	1,617
2022	1,539	1,608
2023	1,491	1,605
2024 - 2028	6,670	8,227

d. Defined Contribution Plans
AFMICSI also sponsors a qualified contributory 401(k) plan (the 401(k) Plan) in which employees of AFMICSI are eligible to participate. Employees who choose to participate in the 401(k) Plan contribute between 1% and 30% of eligible base compensation, subject to IRS limitations. AFMICSI

(in thousands of dollars)

is required to make contributions each payroll period to a trust fund. AFMICSI's contributions are based on a formula with a 100% match on the first 3% of eligible contributions plus 50% on the next 2% of eligible contributions for a maximum annual contribution of 4% of participants' eligible compensation. The Company recognized expense of $25,077 and $22,552 related to the 401(k) Plan in 2018 and 2017, respectively.

PGC sponsors a defined contribution 401(k) plan in which substantially all employees of PGC are eligible to participate (PGC Plan). Under the PGC Plan, PGC's matching contribution is equal to 50% to 100% of each participant's contribution (depending upon years of service) to a maximum of 5% of the participant's eligible compensation. Expenses related to the PGC Plan of $1,700 and $2,464 were incurred during 2018 and 2017, respectively.

Homesite sponsors a defined contribution 401(k) plan in which substantially all Homesite employees 21 or older are eligible to participate (Homesite Plan). Under the Homesite Plan, Homesite's matching contribution is equal to 50% of each participant's contribution, subject to a maximum of 5% of the participant's eligible compensation. Expenses related to the Homesite plan of $7,922 and $7,864 were incurred during 2018 and 2017, respectively.

NGM sponsors a profit-sharing retirement plan for which substantially all NGM employees are eligible. Expenses related to the NGM plan of $481 were incurred during 2018.

A liability of $75,418 and $74,039 was accrued for earned but unpaid compensated absences as of December 31, 2018 and 2017, respectively.

9. Agent Contract Termination Payments

Exclusive agents of the Company are eligible to receive payments upon termination after a period of covered service. Years of service exclude time under an advance compensation plan, not to exceed two years. For agents appointed prior to January 1, 2009 that have more than 10 years of covered service, payments are based on a percentage of service fees during the period of up to 12 months prior to termination (as defined in the agreement). For agents appointed on or after January 1, 2009 that have eight or more years of covered service, payments are based on a cash balance formula that utilizes sales and service fees (as defined in the agreement).

The Company uses a measurement date of December 31 for its agent contract termination payments plan.

The following table reflects components of amounts recognized in the Company's consolidated balance sheets and the accumulated benefit obligation at December 31:

	2018	2017
Projected benefit obligation	$ 780,233	$ 762,347
Fair value of plan assets	—	—
Funded status	$ (780,233)	$ (762,347)
Liabilities:		
Accrued benefit costs	763,688	743,655
Liability for benefits	16,545	18,692
Total liabilities	$ 780,233	$ 762,347
Accumulated benefit obligation	$ 680,046	$ 673,635

(in thousands of dollars)

The following table reflects amounts in accumulated other comprehensive income (loss) that have not yet been recognized as components of net periodic benefit cost at December 31:

	2018	2017
Net transition asset or obligation	$ —	$ —
Net prior service cost or credit	—	—
Net recognized gains and losses	16,545	18,692
Total	$ 16,545	$ 18,692

The following table reflects components of amounts recognized in the Company's consolidated statements of comprehensive income at December 31:

	2018	2017
Net periodic cost	$ 58,219	$ 55,045
Employer contribution	38,186	38,407
Benefits paid	(38,186)	(38,407)

The following table represents components of periodic benefit cost that are recognized in other comprehensive income at December 31, 2018:

Actuarial gain (loss)	$ 2,446
Less: Amortization of actuarial gain (loss)	(299)
Prior service cost	—
Less: Amortization of prior service cost	—
Net transition obligation	—
Less: Amortization of net transition obligation	—
Net recognized in other comprehensive income	$ 2,147

The following table represents estimated amounts to be amortized in next year's net periodic pension cost from accumulated other comprehensive income:

Net actuarial (gain)/loss	$ (300)
Net prior service cost	—
Net transition asset or obligation	—
Total	$ (300)

(in thousands of dollars)

The weighted-average actuarial assumptions used in determining the projected benefit obligations and net periodic benefit cost as of December 31 are as follows:

	2018	2017
Projected benefit obligation:		
Discount rate	4.20%	3.55%
Service fees increase		
AFMICSI		
First 8 years after appointment	n/a	21.00
After first 8 years of appointment	n/a	3.25
First 6 years after appointment	27.75	n/a
Years 7 through 20 after appointment	6.75	n/a
After 20 years of appointment	2.75	n/a
American Standard Insurance Company (ASIC)*		
First 6 years after appointment	8.00	8.00
After first 6 years of appointment	(4.00)	(4.00)
Net periodic benefit cost:		
Discount rate	3.55	4.00
Service fees increase		
AFMICSI		
First 8 years after appointment	21.00	21.00
After first 8 years of appointment	3.25	3.25
ASIC		
First 6 years after appointment	8.00	8.00
After first 6 years of appointment	(4.00)	(4.00)

*ASIC is a subsidiary of AmFam, Inc. which is a subsidiary of AFMICSI

Expected Cash Flows

Information about the expected cash flows for the contract termination payments plan follows:

Expected contract termination payments	
2019	$ 44,099
2020	45,368
2021	49,505
2022	53,253
2023	56,664
2024 - 2028	312,849

The above table reflects vested balances expected to be paid from the Company's assets.

(in thousands of dollars)

10. Property & Casualty Loss and Loss Adjustment Expense Reserve

The Company establishes reserves for losses and loss adjustment expenses on reported and unreported claims of insured losses. Data reviewed in estimating ultimate losses for each coverage include development of paid and incurred losses (gross of salvage and subrogation received), salvage and subrogation received, closed and reported claims and paid and incurred average costs on both an accident-year and accident-quarter basis. Other supplemental reserving methodologies are also considered.

Catastrophe losses are determined on a by-peril basis and are reserved for separately. In addition, large storms with losses greater than $25 million are examined independently of smaller storm events during the reserving process. Data reviewed in estimating ultimate defense and cost containment (D&CC) expenses include incremental paid D&CC expense per exposure triangulations and cumulative paid D&CC expense triangulations on an accident-year basis.

Ultimate claims are determined by examining development of closed and reported claim triangles. Other supplemental reserving methodologies, such as reported claim triangles per exposure or per premium, and incremental claim emergence, are also considered.

Activity in the loss and loss adjustment expense reserve for property & casualty insurance, including health insurance, is summarized as follows:

	2018	2017
Direct and assumed balances as of January 1	$ 4,750,962	$ 4,085,485
Less reinsurance recoverables on unpaid losses and loss adjustment expenses	415,749	42,043
Net balance as of January 1	4,335,213	4,043,442
Net loss and loss adjustment reserves acquired - See Note 2	1,133,371	—
Total beginning reserves	5,468,584	4,043,442
Incurred losses and loss adjustment expenses related to		
Current year	6,961,241	6,311,710
Prior years	(155,445)	12,763
Total incurred	6,805,796	6,324,473
Paid losses and loss adjustment expenses related to		
Current year	4,175,398	4,069,385
Prior year	1,971,912	1,963,317
Total paid	6,147,310	6,032,702
Net balance as of December 31	6,127,070	4,335,213
Plus reinsurance recoverables on unpaid losses and loss adjustment expenses	303,822	415,749
Direct and assumed balance as of December 31	$ 6,430,892	$ 4,750,962

Property & casualty loss and loss adjustment expenses incurred decreased by $155,445 and increased by $12,763 during 2018 and 2017, respectively, attributable to re-estimation of unpaid losses and loss adjustment expenses from insured events of prior years. The lines of business primarily affected were Private Passenger Auto Liability, Auto Physical Damage and Homeowners/Farmowners in 2018 and Private Passenger Auto Liability, Commercial Multiple Peril and Other Liability in 2017.

Increases or decreases of this nature occur as the result of claim settlements during the current year and as additional information is received regarding individual claims, causing changes from the original estimates of individual claims. Recent loss development trends are also taken into account in evaluating the overall adequacy of unpaid losses and loss adjustment expenses.

AFI MHC has environmental exposure from its business owners, other commercial multiple peril, and general liability policies. Since the Company wrote minimal levels of commercial lines business prior to the introduction of the absolute pollution exclusion, reported claim activity levels to date have not been material and the Company's exposure is insignificant.

The following presents information about incurred and paid claims development as of December 31, 2018, net of reinsurance, for significant lines of business. This information includes allocated defense and cost containment expenses while adjusting and other loss adjustment expenses are excluded from presentation as these expenses are generally not allocated to specific claims. The cumulative number of reported claims is identified by coverage and excludes reported claims for industry pools and facilities where information is not available.

The information about incurred and paid claims development for years prior to 2018 and the average annual percentage payout of incurred claims by age as of December 31, 2018 is unaudited and presented as required supplementary information. The tables below incorporate MSAG's claims development information on a retrospective basis for all periods presented in order to provide complete and meaningful information. See Note 2 for more information on the merger with MSAG.

(in thousands of dollars)

Auto insurance

	Incurred claims and allocated claim adjustment expenses, net of reinsurance					IBNR reserves plus expected development on reported claims	Cumulative number of reported claims
	For the years ended December 31,						
	(unaudited)	(unaudited)	(unaudited)	(unaudited)			
Accident year	2014	2015	2016	2017	2018	As of December 31, 2018	
2014	$ 2,670,687	$ 2,603,713	$ 2,547,010	$ 2,539,083	$ 2,542,367	$ 43,160	1,084,416
2015	—	2,707,945	2,730,900	2,707,922	2,699,445	94,334	1,054,516
2016	—	—	3,061,951	2,941,844	2,963,150	177,744	1,120,077
2017	—	—	—	3,438,964	3,441,540	339,112	1,350,215
2018	—	—	—	—	3,719,383	838,136	1,383,678
					$15,365,885		

	Cumulative paid claims and allocated claims adjustment expense, net of reinsurance				
	For the years ended December 31,				
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	
Accident year	2014	2015	2016	2017	2018
2014	$ 1,564,994	$ 2,066,295	$ 2,260,111	$ 2,389,175	$ 2,467,350
2015	—	1,599,112	2,193,743	2,401,115	2,535,183
2016	—	—	1,793,379	2,364,235	2,624,829
2017	—	—	—	2,048,927	2,793,886
2018	—	—	—	—	2,140,887
					$12,562,135
All outstanding liabilities before 2014, net of reinsurance					97,403
Liabilities for claims and claim adjustment expenses, net of reinsurance					$ 2,901,153

Average annual percentage payout of incurred claims by age, net of reinsurance, as of December 31, 2018				
1 year	2 years	3 years	4 years	5 years
59.2%	20.7%	8.3%	5.0%	3.3%

(in thousands of dollars)

Homeowners & farmowners insurance

	Incurred claims and allocated claim adjustment expenses, net of reinsurance					IBNR reserves plus expected development on reported claims	Cumulative number of reported claims
	For the years ended December 31,						
	(unaudited)	(unaudited)	(unaudited)	(unaudited)			
Accident year	**2014**	**2015**	**2016**	**2017**	**2018**	**As of December 31, 2018**	
2014	$ 1,411,757	$ 1,330,849	$ 1,314,751	$ 1,318,330	$ 1,311,382	$ 11,696	238,886
2015	—	1,352,681	1,339,847	1,329,364	1,338,288	14,816	209,165
2016	—	—	1,537,623	1,530,560	1,515,721	30,563	222,211
2017	—	—	—	1,804,551	1,804,640	48,365	215,234
2018	—	—	—	—	2,092,408	203,208	230,539
					$ 8,062,439		

	Cumulative paid claims and allocated claims adjustment expense, net of reinsurance				
	For the years ended December 31,				
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	
Accident year	**2014**	**2015**	**2016**	**2017**	**2018**
2014	$ 1,040,241	$ 1,252,515	$ 1,278,139	$ 1,290,241	$ 1,295,153
2015	—	960,512	1,245,694	1,287,391	1,310,160
2016	—	—	1,054,623	1,411,852	1,460,383
2017	—	—	—	1,465,824	1,679,138
2018	—	—	—	—	1,513,872
					$ 7,258,706
All outstanding liabilities before 2014, net of reinsurance					37,408
Liabilities for claims and claim adjustment expenses, net of reinsurance					$ 841,141

Average annual percentage payout of incurred claims by age, net of reinsurance, as of December 31, 2018				
1 year	2 years	3 years	4 years	5 years
73.7%	19.8%	2.9%	1.4%	0.8%

(in thousands of dollars)

Commercial multiple peril insurance

	Incurred claims and allocated claim adjustment expenses, net of reinsurance						IBNR reserves plus expected development on reported claims	Cumulative number of reported claims
	For the years ended December 31,							
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)			
Accident year	2013	2014	2015	2016	2017	2018	As of December 31, 2018	
2013	$ 433,665	$ 430,400	$ 446,271	$ 472,728	$ 486,293	$ 507,193	$ 30,242	42,201
2014	—	488,214	467,178	495,411	515,898	543,532	44,378	45,386
2015	—	—	435,342	466,677	477,851	519,299	69,087	41,270
2016	—	—	—	463,734	480,061	513,209	104,649	46,310
2017	—	—	—	—	572,130	596,012	153,560	58,730
2018	—	—	—	—	—	571,536	279,279	33,937
						$3,250,781		

	Cumulative paid claims and allocated claims adjustment expense, net of reinsurance					
	For the years ended December 31,					
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	
Accident year	2013	2014	2015	2016	2017	2018
2013	$ 224,568	$ 335,835	$ 376,978	$ 413,505	$ 440,328	$ 459,472
2014	—	263,895	351,029	398,623	445,281	472,111
2015	—	—	207,400	314,880	370,505	408,708
2016	—	—	—	188,444	299,628	358,153
2017	—	—	—	—	257,526	374,799
2018	—	—	—	—	—	209,283
						$2,282,526
All outstanding liabilities before 2013, net of reinsurance						145,393
Liabilities for claims and claim adjustment expenses, net of reinsurance						$1,113,648

Average annual percentage payout of incurred claims by age, net of reinsurance, as of December 31, 2018					
1 year	2 years	3 years	4 years	5 years	6 years
39.3%	19.9%	9.8%	6.9%	4.9%	3.9%

(in thousands of dollars)

The reconciliation of the net incurred and paid claims development tables above to the reserve for property & casualty loss and loss adjustment expense reserve in the consolidated balance sheets as of December 31, 2018 is as follows:

Net outstanding liabilities:	
Auto insurance	$ 2,901,153
Homeowners & farmowners insurance	841,141
Commercial multiple peril insurance	1,113,648
Other insurance	891,195
Adjusting and other loss adjustment expenses	486,109
Fair value adjustment on acquired reserves	(106,176)
Net reserve for property & casualty loss and loss adjustment expense reserve	6,127,070
Reinsurance recoverable:	
Auto insurance	38,274
Homeowners & farmowners insurance	172,582
Commercial multiple peril insurance	35,263
Other insurance	42,030
Adjusting and other loss adjustment expenses	19,398
Fair value adjustment on acquired reinsurance recoverable	(3,725)
Total reinsurance recoverable	303,822
Gross reserve for property & casualty loss and loss adjustment expense reserve	$ 6,430,892

11. Debt

The Company holds three surplus notes issued in 2002, 2003, and 2016. The interest rate on the 2002 note adjusts quarterly based on 90-day London Interbank Offered Rate (LIBOR) plus 4.00%. The interest rate on the 2003 note adjusts quarterly based on 90-day LIBOR plus 4.10%. The interest rate on the 2016 note is fixed at 7.25%. All surplus notes have a stated term of 30 years and are redeemable after five years. The Florida Insurance Commissioner must approve, in advance, interest and principal payments on these surplus notes. These payments are subordinated and junior in right of payment to the prior payment in full of all policy claims and senior indebtedness of the Company. The notes issued in 2002 and 2003 are carried at the unpaid principal balance, while the note issued in 2016 is carried at fair value and is being amortized to the unpaid principal balance.

The Company holds two subordinated debenture obligations issued in 2006 and 2007. The debenture issued in 2006 has a stated term of 30 years redeemable after five years and a floating interest rate adjusted quarterly based on 90-day LIBOR plus 3.00%. The debenture issued in 2007 has a stated term of 30 years redeemable after five years and a floating interest rate adjusted quarterly based on 90-day LIBOR plus 2.95%. These obligations are carried at the unpaid principal balance.

The Company holds two subordinated debenture obligations issued in 2004 with a stated term of 30 years redeemable after five years and a floating interest rate adjusted quarterly based on the 90-day London Interbank Offered Rate (LIBOR). The obligations are carried at the unpaid principal balance.

The Company is a member of the FHLBC. The general nature of the FHLBC agreement is to provide a platform which provides the Company with the ability to receive advances from the FHLBC as a member of the bank. Through its membership, the Company has outstanding a 30-year fixed rate advance that pays monthly interest to FHLBC at a fixed annual interest rate of 5.12%, and principal is due in a balloon payment at the end of the advance's 30-year term. The Company has elected the fair value option for this debt instrument, so carrying value equals fair value (see Note 3(h)). In 2017, the Company executed a 1-year advance and paid monthly interest to the FHLBC at a fixed annual interest rate of 1.95%. All principal was repaid at the end of the advance's 1-year term in 2018. This advance was carried at the unpaid principal balance.

(in thousands of dollars)

The following summarizes the Company's debt as of and for the years ended December 31:

				2018			2017			
Issue Date	Debt Type	Interest Rate	Face Amount	Carry Value	Interest Paid	Interest Accrued	Carry Value	Interest Paid	Interest Accrued	Maturity Date
12/4/2002	Surplus Note	6.74%	$ 15,000	$ 15,000	$ 240	$ —	**	**	**	12/4/2032
5/15/2003	Surplus Note	6.72	15,000	15,000	246	132	**	**	**	5/15/2033
11/2/2016	Surplus Note	7.25	70,000	73,184	—	—	**	**	**	11/2/2036
6/15/2006	Subordinated Debenture	5.79	35,000	36,083	487	87	**	**	**	6/15/2036
6/21/2007	Subordinated Debenture	5.74	30,000	30,928	413	87	**	**	**	6/15/2037
12/15/2004	Subordinated Debenture	2.81	36,083	36,083	2,007	—	$ 36,083	$ 1,666	$ —	12/15/2034
11/20/2013	FHLBC Fixed Rate Advance	5.12	500,000	606,920	25,956	2,204	647,566	25,956	2,204	11/20/2043
12/14/2017	FHLBC Fixed Rate Advance	1.95	130,000	—	2,479	92	130,000	—	127	12/14/2018
	Other			167			356			
			$ 831,083	$ 813,365	$ 31,828	$ 2,602	$ 814,005	$ 27,622	$ 2,331	

** These debt instruments were acquired on October 31, 2018 as part of the merger with MSAG, thus there are no balances reflected in this table as of and for the year ended December 31, 2017; see Note 2

12. Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) at December 31 was comprised of the following components:

	2018	2017
Unrealized gains (losses) on common stocks	$ 540,767	$ 990,877
Unrealized gains (losses) on bonds	(45,600)	225,354
Unrealized gains (losses) on other assets	1,008	1,008
Adjustment of DAC relating to fair value adjustment	7,900	(32,428)
Post-retirement benefit obligations	(265,491)	(280,593)
Agent contract termination payment obligation	(16,545)	(18,692)
Deferred income taxes	(42,874)	(302,871)
Accumulated other comprehensive income (loss)	$ 179,165	$ 582,655

13. Separate Accounts

Separate account assets include segregated funds invested by the Company for the benefit of VUL and VA policy owners. Policy owners' premium payments, net of applicable loads, are invested in accordance with selections made by the policy owner into the Variable Accounts. The Company records these payments as assets in the separate accounts. Separate account liabilities represent reserves held related to the separate account business.

(in thousands of dollars)

The Variable Accounts are unit investment trusts registered under the Investment Company Act of 1940. Each Variable Account has ten subaccounts, each of which invests in a non-proprietary mutual fund (the Fund). The shares of the Funds are carried at the net asset value of the Funds, which approximates fair value.

A fixed account is also included as an investment option for variable policy owners. Premiums, net of applicable loads, allocated to the fixed account are invested in the general assets of the Company.

The assets and liabilities of the Variable Accounts are clearly identified and distinguished from the other assets and liabilities of the Company. The assets of the Variable Accounts will not be applied to the liabilities arising out of any other business conducted by the Company.

The Company assumes the mortality and expense risk associated with these contracts and therefore deducts a daily mortality and expense charge from the assets of the separate accounts. Income from these charges is included in premium revenues in the consolidated statements of comprehensive income, and is 100% ceded to a third party. The charges to the separate accounts, shown as follows for the years ended December 31, are based on the average daily net assets at specified annual rates:

	2018	2017
American Family Variable Account I	$ 773	$ 841
American Family Variable Account II	1,861	1,846
	$ 2,634	$ 2,687

In addition, the Company deducts certain amounts from the cash value of the accounts invested in the separate accounts for surrender charges, annual administrative charges, and cost of insurance charges. Income from these charges is included in premium revenues in the consolidated statements of comprehensive income, and is 100% ceded to a third party. For the years ended December 31, amounts are as follows:

	2018	2017
American Family Variable Account I	$ 9,679	$ 10,001
American Family Variable Account II	221	190
	$ 9,900	$ 10,191

14. Statutory Financial Data

The Company's insurance subsidiaries also prepare financial statements in accordance with statutory accounting (STAT) practices prescribed or permitted by the state of Wisconsin, Illinois, California, Georgia, New York, Texas, Florida, South Carolina, Indiana, and Minnesota (collectively the Companies' operating NAIC states). Prescribed STAT practices include the NAIC's "Accounting Practices and Procedures Manual," state laws, regulations, and general administrative rules applicable to all insurance enterprises domiciled in a particular state. In addition, the Companies' operating NAIC states have a right to permit other specific practices that may deviate from prescribed practices. No permitted differences in STAT practices between the Companies' operating NAIC states and the NAIC are used in the preparation of the statutory financial statements. Financial statements prepared in accordance with STAT vary materially from financial statements prepared in conformity with GAAP.

The Company's insurance subsidiaries are subject to regulation and supervision by the various state insurance regulatory authorities in the states in which they conduct business. Such regulation is generally designed to protect policyholders and includes such matters as maintenance of minimum statutory capital and surplus, risk-based capital ratios, and restrictions on the payment of policyholder dividends. Generally, a portion of the Company's insurance subsidiaries' statutory surplus may be available for distribution to shareholders. However, such distributions as dividends may be subject to prior regulatory approval.