



Torchmark
Corporation 

ANNUAL REPORT 2017

PRINCIPAL EXECUTIVE OFFICE

3700 South Stonebridge Drive
McKinney, Texas 75070
(972) 569-4000

**ANNUAL MEETING
OF SHAREHOLDERS**

10:00 a.m. CDT, Thursday, April 26, 2018
Corporate Headquarters
3700 South Stonebridge Drive
McKinney, Texas 75070

The proceedings will be webcast live and in replay on the Investors page of the Torchmark Corporation website. The Company's Annual Meeting will be conducted in accordance with its Shareholder Rights Policy. A copy of this policy can be obtained on the Company's website, or by contacting the Corporate Secretary at the Torchmark Corporation headquarters address.

INVESTOR RELATIONS

Contact: Mike Majors
Phone: (972) 569-3239
Fax: (972) 569-3282
Email: tmkir@torchmarkcorp.com

**INDEPENDENT REGISTERED PUBLIC
ACCOUNTANTS**

Deloitte & Touche LLP
2200 Ross Avenue
Suite 1600
Dallas, Texas 75201

STOCK EXCHANGE LISTINGS

New York Stock Exchange
Symbol: TMK

**INDENTURE TRUSTEE FOR
9¼%, 7½%, AND 3.8% SENIOR NOTES
AND 6½% AND 5¼% JUNIOR
SUBORDINATED DEBENTURES**

Regions Bank
Corporate Trust Services
3773 Richmond Ave., Suite 1100
Houston, TX 77046-3703
PHONE: (713) 244-8043
WEB: https://www.regions.com/commercial_banking/corp_trust.rf
The 6½% debentures trade through Depository Trust Company under global certificates listed on the New York Stock Exchange (NYSE Symbol TMKPRC). The 5¼% debentures trade through Depository Trust Company under global certificates listed on the Singapore Stock Exchange.

**STOCK TRANSFER AGENT AND SHAREHOLDER
ASSISTANCE**

EQ Shareowner Services
P.O. Box 64854
St. Paul, MN 55164-0854
or
1110 Centre Pointe Curve, Suite 101
Mendota Heights, MN 55120-4100
Toll-Free Number: (866) 557-8699
TDD: Hearing impaired can use a relay service
Outside the U.S.: (651) 450-4064
Website: www.shareowneronline.com

DIVIDEND REINVESTMENT

Torchmark maintains a dividend reinvestment plan for all holders of its common stock. Under the plan, shareholders may reinvest all or part of their dividends in additional shares of common stock and may also make periodic additional cash payments of up to \$3,000 toward the purchase of Torchmark stock. Participation is voluntary. More information on the plan may be obtained from the Stock Transfer Agent by calling toll-free (866) 557-8699 or by writing: Torchmark Corporation, c/o EQ Shareowner Services, P.O. Box 64874, St. Paul, MN 55164-0874 or 1110 Centre Pointe Curve, Suite 101, Mendota Heights, MN 55120-4100.

**AUTOMATIC DEPOSIT
OF DIVIDENDS**

Automatic deposit of dividends is available to shareholders who wish to have their dividends directly deposited into the financial institution of their choice. Authorization forms may be obtained from the Stock Transfer Agent by calling toll-free (866) 557-8699.

TORCHMARK CORPORATION WEBSITE

On the www.torchmarkcorp.com home page are links to the web pages of:

- Company**
- Brands**
- Careers**
- Community**
- Investors**
- Contact**

The Investors page contains a menu with links to many topics of interest to investors and other interested third parties:

- Annual Reports, 10-K and Proxy Statements**
- Calendar**
- News Releases**
- SEC Filings**
- XBRL**
- Financial Reports and Other**

Financial Information

**Environmental, Social and
Governance Report**

Investor Contact Information

Calls and Meetings

- Management Presentations
- Conference Calls on the Web
- Conference Call Replays and Transcripts
- Annual Meeting of Shareholders

Stock Information

- Stock Transfer Agent and Shareholder Assistance
- Dividend Reinvestment
- Automatic Deposit of Dividends

Corporate Governance

- Shareholders' Rights Policy

- Code of Business Conduct and Ethics
- Corporate By-laws
- Code of Ethics for CEO and Senior Financial Officers
- Corporate Governance Guidelines
- Related Party Transaction Policy
- Employee Complaint Procedures

Board of Directors

- Members of the Board
- Committees
 - Audit Committee
 - Compensation Committee
 - Governance and Nominating Committee
- Executive Sessions
- Director Qualification Standards
- Director Independence Criteria
- Director Resignation Policy

2017 IN FOCUS

\$ in thousands

\$3,282,935

Total Premium From Continuing Operations

\$573,681

Net Operating Income From Continuing Operations

\$2,373,099

Annualized Life Premium In Force

\$1,018,020

Annualized Health Premium In Force



FINANCIAL HIGHLIGHTS

\$ in thousands, except per share amounts

	2017	2016	% CHANGE
OPERATIONS			
Total Premium From Continuing Operations	\$3,282,935	\$3,137,034	4.7 ↑
Net Operating Income From Continuing Operations ¹	573,681	549,360	4.4 ↑
Net Income	1,454,494 ⁺	549,779	+
Annualized Life Premium In Force	2,373,099	2,262,736	4.9 ↑
Annualized Health Premium In Force	1,018,020	998,634	1.9 ↑
Diluted Average Shares Outstanding	118,983	122,368	2.8 ↓
Net Operating Income From All Operations as a Return on Average Equity (excluding net unrealized gains on fixed maturities ¹)	14.3%	14.6%	
PER COMMON SHARE (ON A DILUTED BASIS)			
Net Operating Income From Continuing Operations ¹	\$4.82	\$4.49	7.3 ↑
Shareholders' Equity (excluding net unrealized gains on fixed maturities ¹)	39.77 ⁺	32.13	23.8 ↑

¹The following financial measures utilized by management and contained in the following Letter to Shareholders are considered non-GAAP: net operating income; net operating income as a return on average equity, excluding net unrealized gains on fixed maturities; book value (shareholders' equity) per share, excluding net unrealized gains or losses on fixed maturities; underwriting income or margin (consolidated). Torchmark includes non-GAAP measures to enhance investors' understanding of management's view of the business. The non-GAAP measures are not a substitute for GAAP, but rather a supplement to increase transparency by providing broader perspective. Torchmark's definitions of non-GAAP measures may differ from other companies' definitions. Reconciliations to GAAP financial data are presented on pages 14-15.

⁺As a result of the tax reform legislation enacted in 2017, the Company made a one-time adjustment of \$874 million to net income. Excluding the tax reform adjustment, net income and shareholders' equity, excluding net unrealized gains on fixed maturities, would have been \$581 million and \$34.68, respectively.



“We believe Torchmark has a very bright future. Many times we hear that life insurance is a mature market with limited growth potential. For Torchmark, this is simply not true. We are uniquely positioned to thrive and build shareholder value well into the future.”



LETTER TO SHAREHOLDERS*

Torchmark had another good year in 2017. Return on equity, excluding net unrealized gains on fixed maturities, was 14.3% and total premiums grew 5%. Agency sales grew 8%, driven by increases in both agent count and productivity. We have had sales growth in each of our exclusive agencies now for four years in a row. While Direct Response sales have declined, this was by design due to actions taken to maximize profit dollars. We are encouraged with recent results as we have seen the margins stabilize. We expect to begin to see Direct Response sales growth again in 2019.

Many investors ask us how Torchmark differs from other life insurance companies. The answer can be found in our business model, a model that has consistently facilitated significant growth regardless of general economic conditions. The components of this model are discussed below:



MARKET

We serve working families in niches of the middle-income market – a vastly underserved marketplace with significant growth potential and relatively little competition.



CONTROLLED DISTRIBUTION

We market our products primarily through exclusive agency and direct response channels. This enhances our ability to limit competitive pressures and control costs.



CASH FLOWS

Torchmark's highly persistent block of in force business produces strong excess cash flows year in and year out. The persistency of our in force block has always been very stable, regardless of macro-economic conditions. Nearly 90% of our premium revenue comes from policies sold in prior years.



PRODUCTS

We focus on basic life and supplemental health products that best meet the needs of our marketplace. These products are simple for agents and customers to understand and are not impacted by interest rate or equity market fluctuations.



MARGINS

Torchmark has a long history of administrative efficiency. Our ability to control both acquisition and administrative costs helps produce healthy underwriting margins. As such, we don't have to rely on investment income to generate operating income.



RETURN OF EXCESS CAPITAL TO SHAREHOLDERS

Due to the significant amount of excess cash flow produced each year, Torchmark has returned approximately 71% of its net income to shareholders through share repurchases and dividends since 1986 (absent the positive impact that tax reform had on 2017 net income, this ratio would be 76%). We remain committed to returning excess capital to shareholders.

*Throughout this letter net operating income represents net operating income from continuing operations.

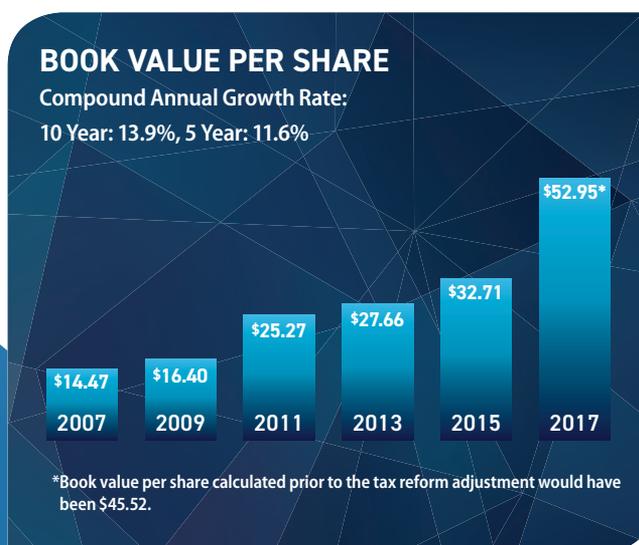
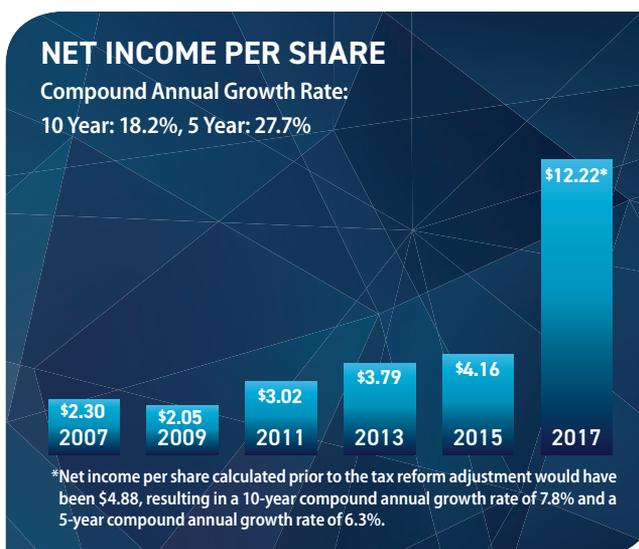
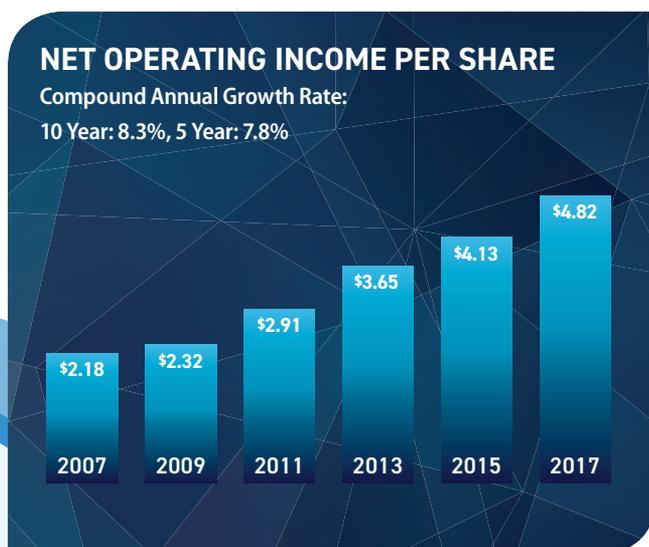
We will continue to follow this business model. That being said, we must continually refine that model through innovation and the use of technology in response to the changing needs and expectations of our agents and customers. It is imperative that we work with customers and agents in a manner that best meets their needs and preferences.

In order to ensure that we maximize our ability to be nimble and adapt to a rapidly changing environment, we continue to make significant investments in technology. These investments are designed with the following goals in mind:

- Facilitate a digital consumer experience
- Improve the agent experience and ease of doing business
- Replace back office legacy systems with modern, commercial solutions
- Expand the use of data analytics
- Protect against cyber threats

While these investments require significant resources and attention, we believe they are a critical component of profitable future growth.

Torchmark has produced steady growth in earnings per share and book value per share as evidenced by the charts below.



Torchmark consistently generates a strong return on equity (ROE). In 2017, the ROE, excluding net unrealized gains on fixed maturities, was 14.3%. On a GAAP basis, 2017 ROE was 28.2%. The higher GAAP level was due primarily to the impact of tax reform.

INSURANCE OPERATIONS

COMPONENTS OF NET OPERATING INCOME

(\$ in millions, except per share data)

		PER SHARE
Underwriting Income	\$625	\$5.25
Excess Investment Income	239	2.01
Tax and Parent Expenses	(288)	(2.42)
Stock Compensation Expense, Net of Tax	(2)	(0.02)
Net Operating Income	\$574	\$4.82

Underwriting income reflects premiums less policy benefits, acquisition costs, and administrative expenses. In contrast to many other life insurance companies, most of Torchmark's operating income is generated by insurance underwriting margin, rather than investment income. Underwriting income accounted for approximately 73% of pre-tax operating income in 2017.



COMPONENTS OF UNDERWRITING INCOME

(\$ in millions)

	\$	AS % OF PREMIUM
Underwriting Margin		
Life	\$604	26.2%
Health	219	22.5%
Other	11	
Total	\$834	25.4%
Administrative Expenses Net of Other Income	(209)	6.4%
Underwriting Income	\$625	19.0%

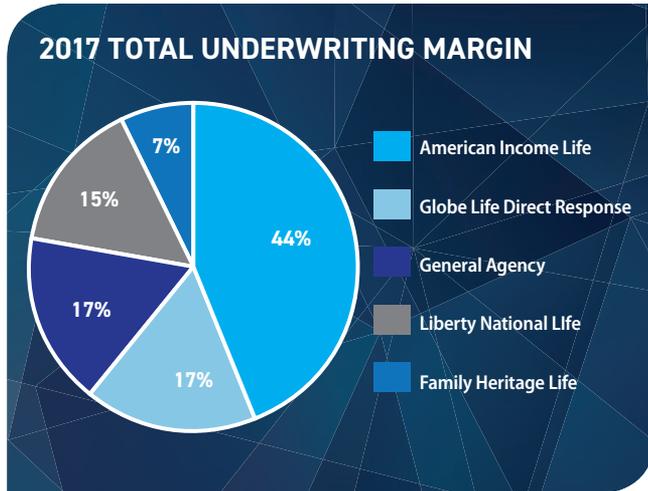
We prefer to focus on basic protection life insurance and supplemental health insurance products that provide more predictable profitability and better meet the needs of our market than other types of coverage. Our products provide protection to families against loss of income due to the death or illness of a breadwinner by helping with final expenses, mortgage payments, tuition or other household expenses.



DISTRIBUTION CHANNELS

We reach the market through several distinct channels, each serving a particular niche.

The chart below shows the distribution of underwriting margin among our distribution channels.



AMERICAN INCOME LIFE

As can be seen in the charts below, American Income has a long history of impressive sales and agent count growth. In addition, life premiums have grown at an 8.5% compound annual growth rate over the past ten years.

For more than 50 years, American Income has operated as an all-union company with a unionized labor force. Through a strong relationship with organized labor, American Income enjoys a natural affinity with the market it serves – working families. While the union affiliation is core to the American Income business, we have diversified over the years through a strong push to focus on other sources of leads such as referrals.

We believe American Income has the potential for significant future growth due to its unique competitive position in an underserved market and its proven ability to grow the agency force.

AMERICAN INCOME LIFE - LIFE SALES

(\$ in millions)

10-Year Compound Annual Growth Rate: 9.3%



AMERICAN INCOME LIFE - AGENT COUNT

10-Year Compound Annual Growth Rate: 10.5%



LIBERTY NATIONAL LIFE

Over the last several years, Liberty National has been transformed from a fixed-cost home service model to a variable-cost model. After a long history of flat to declining life premiums, we believe Liberty National is positioned for sustainable growth. Life premiums grew 2% in 2017, the first annual increase since 2003.

As can be seen below, total sales and agent counts have grown at a compound annual growth rate of 7% and 8%, respectively, over the past five years. This growth is being driven by development of agency middle management that is responsible for the recruiting and training of new agents. We are encouraged by the turnaround at Liberty National and are very optimistic regarding Liberty National's long-term growth prospects.

FAMILY HERITAGE LIFE

Family Heritage primarily markets limited-benefit health products in non-urban areas through a door-to-door approach. Most of these products include a return of premium feature that generates better persistency, margins and investment income than typical health insurance products.

Family Heritage was purchased by Torchmark late in 2012. Since 2013, health sales and agent count have grown 7% and 9%, respectively, driven by incorporation of Torchmark recruiting programs and a focus on agency development. We expect to see consistent growth as Family Heritage continues to incorporate best practices of other Torchmark agencies and cultivate an agency culture centered on recruiting and development of agency middle management.

LIBERTY NATIONAL LIFE - SALES

(\$ in millions)

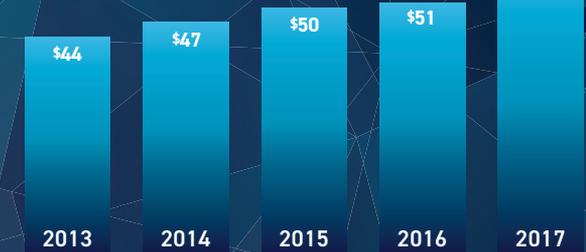
5-Year Compound Annual Growth Rate: 7.3%



FAMILY HERITAGE LIFE - HEALTH SALES

(\$ in millions)

4-Year Compound Annual Growth Rate: 6.7%



LIBERTY NATIONAL LIFE - AGENT COUNT

5-Year Compound Annual Growth Rate: 8.2%



FAMILY HERITAGE LIFE - AGENT COUNT

5-Year Compound Annual Growth Rate: 8.9%



GLOBE LIFE DIRECT RESPONSE

This unit began operations over 50 years ago as a direct mail-only distribution channel. Over the years, we have transitioned to a multifaceted approach, with the addition of insert media and electronic media distribution. Having multiple direct response channels provides us a unique competitive niche in the direct response market because it gives us more ways to monetize leads and allows us to reach consumers more effectively.

While Direct Response has a long history of sales growth, sales have declined in the past couple of years due to operational changes that have been made in response to higher than originally expected claims which emerged in 2015 in certain blocks of business. These operational changes were designed to maximize margin dollars, knowing that sales would be negatively impacted. We expect to begin to grow sales in 2019 through further use of analytics and innovation. However, our primary focus will continue to be the maximization of profit dollars, rather than sales levels.

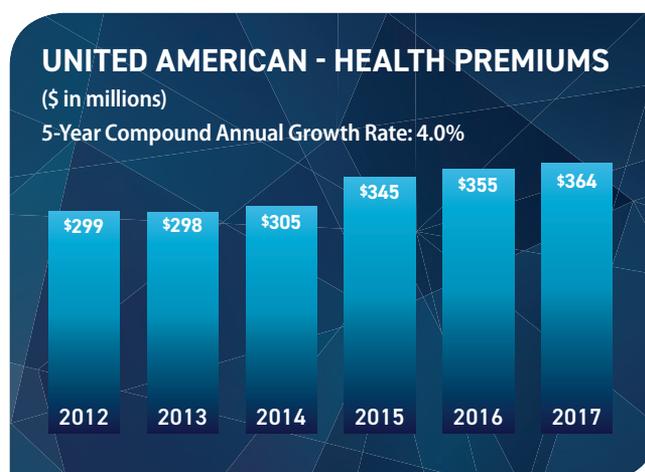
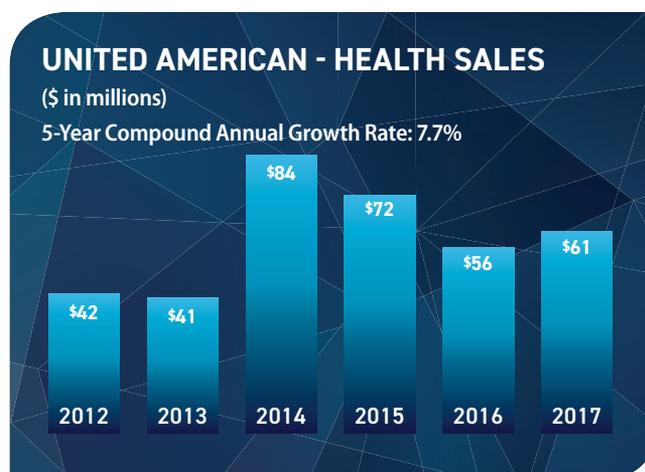
The value of the Direct Response unit extends far beyond direct response sales production. The expertise and resources of this unit also support the recruiting, lead generation and data management efforts of our agencies. We expect Direct Response to continue to help drive Torchmark's success well into the future.



UNITED AMERICAN

This unit primarily markets Medicare Supplement insurance through independent agents and brokers to individuals as well as union and employer groups. The Medicare Supplement market is very different than the markets we serve through controlled distribution. It is a highly regulated, competitive market that is relatively easy for companies to enter and exit. While short-term sales trends are difficult to predict because of the use of independent distribution and the impact of adding large groups, this unit has a relatively stable in force block that continues to grow as shown in the chart below.

We have been in the Medicare Supplement market since the inception of Medicare. We have the expertise and the infrastructure to administer this business efficiently. The use of independent producers allows us to take advantage of opportunity when market conditions are favorable and avoid competitive pressure when market conditions are not as favorable.



INVESTMENT OPERATIONS

COMPONENTS OF NET OPERATING INCOME

(\$ in millions, except per share data)

		PER SHARE
Underwriting Income	\$625	\$5.25
Excess Investment Income	239	2.01
Tax and Parent Expenses	(288)	(2.42)
Stock Compensation Expense, Net of Tax	(2)	(0.02)
Net Operating Income	\$574	\$4.82

We evaluate the investment function on a stand-alone basis rather than allocating investment income to the insurance operations. Excess investment income is the measure used to evaluate the performance of the investment segment. The components of excess investment income can be seen in the chart above. Excess investment income produced 28% of our pre-tax operating income in 2017.

EXCESS INVESTMENT INCOME

(\$ in millions)

Net Investment Income	\$848
Required Interest on Net Policy Liabilities	(524)
Interest on Debt	(85)
Excess Investment Income	\$239

In recent years, growth in excess investment income has been limited by the low interest rate environment. We are encouraged by the prospect of a higher long-term interest rate environment as it would provide higher excess investment income because of the positive impact on net investment income.

INVESTMENT PORTFOLIO

INVESTMENT PORTFOLIO - DECEMBER 31, 2017

Invested Assets (\$ in millions)

	\$	AS % OF TOTAL
Fixed Maturities (at amortized cost)	\$14,995	95%
Policy Loans	530	3
Other Investments	235	2
Total	\$15,760	100%

The strength of our underwriting margins allows us to maintain a conservative philosophy and not make risky bets on investments. While we seek to maximize risk-adjusted returns, the most important criteria when considering new investments is preservation of principal.

We choose to invest almost exclusively in long-term fixed maturities as these fixed-rate investments best match our long term fixed-rate liabilities and enhance our ability to manage capital as efficiently as possible.

TOTAL INVESTED ASSETS AT AMORTIZED COST

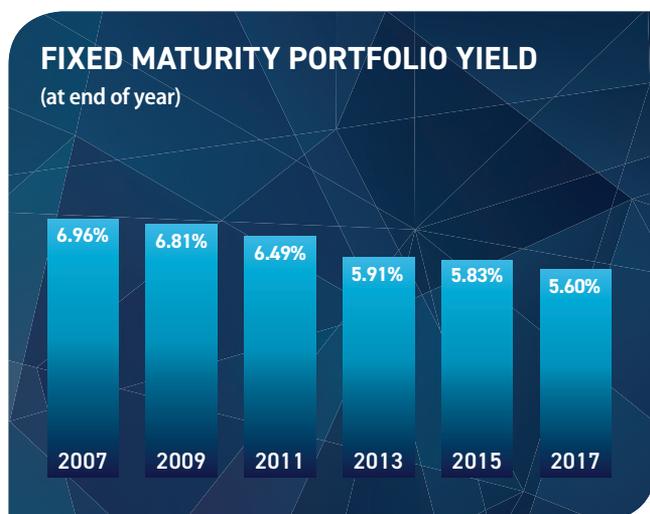
(\$ in billions)

10-Year Compound Annual Growth Rate: 5.6%



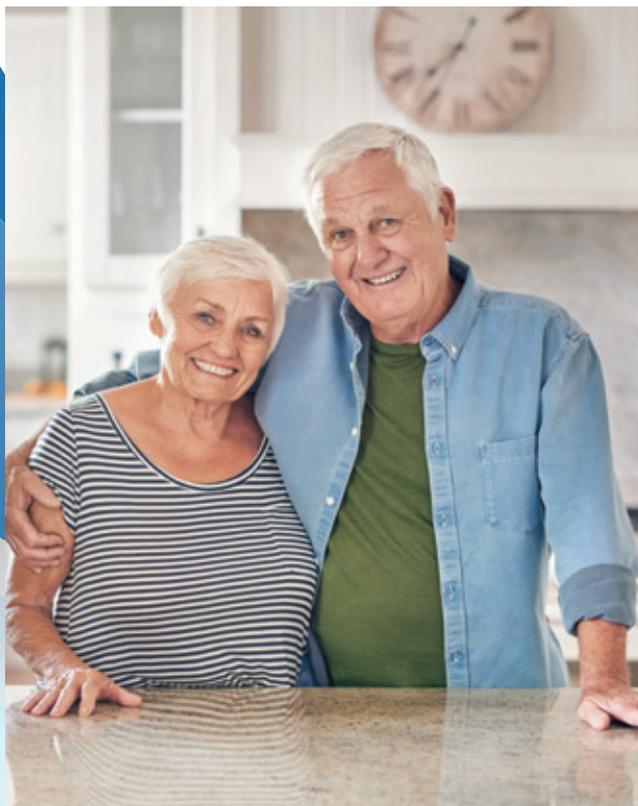
As can be seen in the chart above, invested assets have grown from about \$9 billion at the end of 2007 to just under \$16 billion. This growth was achieved in spite of the fact that we spent \$4.0 billion to repurchase shares over that period.

FIXED MATURITY PORTFOLIO YIELD



This chart demonstrates the negative impact of lower interest rates on investment yields over the last ten years. As we indicated earlier, we hope for higher interest rates – the sooner the better. We are not concerned about the possibility of unrealized losses resulting from higher interest rates as we have the intent and more importantly, the ability, to hold our investments to maturity.

However, if rates don't rise as anticipated, we can continue to thrive in a low interest rate environment as our products are not sensitive to interest rate or equity market fluctuations.

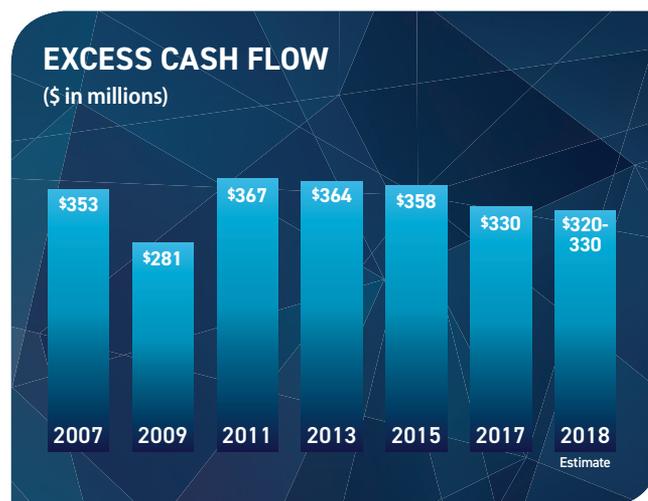


CAPITAL MANAGEMENT

Simply put, our capital management goals are to fully fund operations, maintain appropriate capital levels, and maximize both the amount of and return on excess cash flow.

We define excess cash flow as the cash available to the parent company from the dividends received from the insurance subsidiaries to the parent **after** paying dividends to Torchmark shareholders **and** interest on debt.

The next chart illustrates the significant excess cash flow generated routinely at Torchmark.



Excess cash flow has been somewhat lower in the last couple of years due to slight declines in net statutory income. These declines have resulted in part from the strong life sales growth in recent years and investments in technology discussed earlier. While life sales growth and these technology investments are detrimental to statutory net income in the short run, they will produce growth in excess cash flow in the long run.

SHARE REPURCHASES

	TOTAL SPENT (IN MILLIONS)	NO. OF SHARES (IN 000'S)	AVERAGE PRICE	P/E RATIO*
2008	\$427	17,185	\$24.83	10.9
2009	\$47	4,613	\$10.12	4.4
2010	\$204	8,560	\$23.78	9.4
2011	\$788	28,347	\$27.78	9.5
2012	\$360	11,219	\$32.13	9.7
2013	\$360	8,280	\$43.48	11.9
2014	\$375	7,155	\$52.42	13.4
2015	\$359	6,292	\$56.99	13.8
2016	\$311	5,208	\$59.78	13.3
2017	\$325	4,126	\$78.67	16.3

*Ratios were calculated using net operating income.

Our share repurchase program has been in place now for over 30 years. During that time, there has only been one year in which we did not repurchase stock. That was in 1995 due to the acquisition of American Income. Since 1986, we have spent \$7.1 billion to repurchase 79% of the outstanding shares of the Company.



Returning excess capital to shareholders is core to our business model. As noted earlier, we have returned approximately 71% of our net income to shareholders through dividends and share repurchases since 1986. While share repurchases have been the most efficient use of excess capital over the years, we continually evaluate alternative uses to help ensure we maximize shareholder value.

RETURN TO SHAREHOLDERS

(\$ in millions)

	SHARE REPURCHASES	DIVIDENDS PAID	(A) TOTAL CASH RETURNED	(B) NET INCOME	(A)/ (B)
2008	\$427	\$49	\$476	\$427	111%
2009	\$47	\$47	\$94	\$383	25%
2010	\$204	\$50	\$254	\$499	51%
2011	\$788	\$49	\$837	\$497	168%
2012	\$360	\$56	\$416	\$529	79%
2013	\$360	\$61	\$421	\$528	80%
2014	\$375	\$65	\$440	\$543	81%
2015	\$359	\$67	\$426	\$527	81%
2016	\$311	\$67	\$378	\$550	69%
		Subtotal	\$3,742	\$4,483	83%
2017	\$325	\$69	\$394	\$1,454*	27%*
		10-Year Total	\$4,136	\$5,937	70%

* The Company made a one-time adjustment to 2017 net income as a result of re-measuring deferred tax assets and liabilities at the newly enacted corporate rate. Excluding the tax reform adjustment, the ratio of total cash returned to net income would have been 68% in 2017 and 82% over the past ten years.

TAX REFORM

We want to add our thoughts here regarding the impact of the tax reform legislation recently enacted. Overall, tax reform will be very positive for Torchmark in the long term due to taxation of future profits at the new 21% tax rate. However, due to various other provisions in the new law that impact taxable income, we anticipate our cash tax savings in the short term from the new law will only be about \$5 million to \$10 million per year. Over time we will begin to see more benefit.

The impact of tax reform on required capital levels is yet to be determined. Regardless of the positions the rating agencies and regulators eventually take on this issue, we have a great deal of flexibility. We plan to take actions that will be in Torchmark's best interests and will provide the best overall value for our shareholders.

CONCLUSION

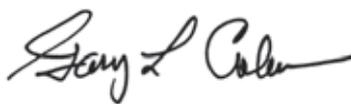
We believe Torchmark has a very bright future. Many times we hear that life insurance is a mature market with limited growth potential. For Torchmark, this is simply not true. There is great need for our products in the middle-income market. Our task is to further reach out and demonstrate that need to potential customers as we grow our distribution channels.

We have essentially been selling the same products in the same markets for the past fifty years and the need for our products today is greater than ever. Due to the tremendous amount of data and experience Torchmark possesses with these products and this market, we are uniquely positioned to thrive and build shareholder value well into the future.

Thank you for your investment in Torchmark.



LARRY M. HUTCHISON
Co-Chairman and
Chief Executive Officer



GARY L. COLEMAN
Co-Chairman and
Chief Executive Officer

Note: Torchmark cautions you that this Letter to Shareholders may contain forward-looking statements within the meaning of the federal securities law. These prospective statements reflect management's current expectations, but are not guarantees of future performance. Accordingly, please refer to Torchmark's cautionary statement regarding forward-looking statements and the business environment in which the Company operates, contained in the Company's Form 10-K for the period ended December 31, 2017, found on the following pages and on file with the Securities and Exchange Commission. Torchmark specifically disclaims any obligation to update or revise any forward-looking statement because of new information, future developments, or otherwise.

DIRECTORS

CHARLES E. ADAIR

President of Kowaliga Capital
Montgomery, Alabama

LINDA L. ADDISON

Immediate Past Managing Partner and Former Chair of the
US Management Committee of Norton Rose Fulbright US LLP
Houston, Texas

MARILYN A. ALEXANDER

Principal of Alexander and Friedman, LLC
Laguna Beach, California

CHERYL D. ALSTON

Executive Director and Chief Investment Officer of
Employees' Retirement Fund of the City of Dallas
Frisco, Texas

DAVID L. BOREN

President of the University of Oklahoma
Norman, Oklahoma

JANE M. BUCHAN

Chief Executive Officer and Managing Director of Pacific
Alternative Asset Management Company, LLC;
Co-Chief Executive Officer of PAAMCO Prisma Holdings
Irvine, California

GARY L. COLEMAN

Co-Chairman and Chief Executive
Officer of Torchmark

LARRY M. HUTCHISON

Co-Chairman and Chief Executive
Officer of Torchmark

ROBERT W. INGRAM

Retired Ross-Culverhouse Professor of Accounting in
Culverhouse College of Commerce, University of Alabama
Gulf Breeze, Florida

STEVEN P. JOHNSON

Retired Partner, Deloitte and Touche, LLP
Plano, Texas

LLOYD W. NEWTON

Retired Executive Vice President
Military Engines of Pratt & Whitney;
Retired General, United States Air Force
Tampa, Florida

DARREN M. REBELEZ

President of International House
of Pancakes, LLC
Glendale, California

LAMAR C. SMITH

Director and Majority Owner of Coles Bay Capital LLC;
Retired Chief Executive Officer of
First Command Financial Services, Inc.
Fort Worth, Texas

MARY E. THIGPEN

Chief Executive Officer and Director of OpsDataStore
Alpharetta, Georgia

PAUL J. ZUCCONI

Retired Partner of KPMG LLP
Plano, Texas

OFFICERS

GARY L. COLEMAN

Co-Chairman and Chief Executive Officer

LARRY M. HUTCHISON

Co-Chairman and Chief Executive Officer

J. MATTHEW DARDEN

Executive Vice President and Chief Strategy Officer

JENNIFER A. HAWORTH

Vice President, Marketing

MARY ELIZABETH HENDERSON

Vice President, Enterprise Lead Generation

VERN D. HERBEL

Executive Vice President and
Chief Administrative Officer

BEN W. LUTEK

Executive Vice President and
Chief Actuary

MICHAEL C. MAJORS

Vice President, Investor Relations

CAROL A. MCCOY

Vice President, Associate Counsel
and Corporate Secretary

JAMES E. MCPARTLAND

Executive Vice President and
Chief Information Officer

R. BRIAN MITCHELL

Executive Vice President,
General Counsel and Chief Risk Officer

CHRISTOPHER T. MOORE

Assistant Secretary

W. MICHAEL PRESSLEY

Executive Vice President and
Chief Investment Officer

JOEL P. SCARBOROUGH

Assistant Secretary

FRANK M. SVOBODA

Executive Vice President and
Chief Financial Officer

REBECCA E. ZORN

Assistant Secretary and Director of Human Resources

DISTRIBUTION OFFICERS

AMERICAN INCOME LIFE

STEVEN K. GREER

Chief Executive Officer, ALL Agency Division

FAMILY HERITAGE LIFE

KENNETH J. MATSON

President and Chief Executive Officer, FHL Agency Division

GLOBE LIFE DIRECT RESPONSE

BILL E. LEAVELL

President and Chief Executive Officer,
Globe Life Direct Response

LIBERTY NATIONAL LIFE

STEVEN J. DICHIARO

Chief Executive Officer, LNL Agency Division

UNITED AMERICAN

MICHAEL C. MAJORS

President

OPERATING SUMMARY

Unaudited and \$ in thousands except per share amounts

	Twelve months ended December 31,		% Increase or Decrease
	2017	2016	
UNDERWRITING INCOME			
Life:			
Premium	\$2,306,547	\$2,189,333	5 ↑
Net policy obligations	(942,595)	(897,650)	
Nondeferred commissions and amortization	(693,693)	(656,869)	
Nondeferred acquisition expense	(65,922)	(61,052)	
Underwriting margin	604,337	573,762	5 ↑
Health:			
Premium	976,373	947,663	3 ↑
Net policy obligations	(550,848)	(539,343)	
Nondeferred commissions and amortization	(183,787)	(176,785)	
Nondeferred acquisition expense	(22,230)	(21,479)	
Underwriting margin	219,508	210,056	4 ↑
Annuity underwriting margin	10,562	9,394	
Total underwriting margin	834,407	793,212	
Other income	1,270	1,534	
Insurance administration expenses	(210,590)	(196,598)	7 ↑
Underwriting income	625,087	598,148	5 ↑
EXCESS INVESTMENT INCOME			
Net investment income	847,885	806,903	5 ↑
Required interest on:			
Net policy liabilities:			
Policy reserves	(734,370)	(702,340)	
Deferred acquisition costs	210,380	202,813	
Debt	(84,532)	(83,345)	
Total excess investment income	239,363	224,031	7 ↑
Corporate expenses	(9,631)	(8,587)	
Pre-tax operating income	854,819	813,592	5 ↑
Income tax	(278,812)	(265,773)	
Net operating income before stock compensation expense	576,007	547,819	
Stock compensation expense, net of tax	(2,326)	1,541	
NET OPERATING INCOME FROM CONTINUING OPERATIONS	\$573,681	\$549,360	4 ↑
Operating EPS from continuing operations on a diluted basis	\$4.82	\$4.49	7 ↑
Discontinued operations - Part D	0	9,033	
Net operating income	\$573,681	\$558,393	3 ↑
Operating EPS on a diluted basis	\$4.82	\$4.56	6 ↑
Diluted average shares outstanding	118,983	122,368	
Reconciliation of Net Operating Income to Net Income:			
Net operating income	\$573,681	\$558,393	
Non operating items, net of tax:			
Realized gains/(losses) - investments	17,590	(6,944)	
Part D adjustments - discontinued operations	(3,769)	1,156	
Administrative settlements	(5,628)	(2,467)	
Non-operating fees	(187)	(359)	
Guaranty fund assessment	(1,171)	0	
Tax reform adjustment	873,978	0	
NET INCOME	\$1,454,494	\$549,779	
EPS on a diluted basis	\$12.22	\$4.49	

The Operating Summary has been prepared in the manner Torchmark management uses to evaluate the operating results of the Company. It differs from the Consolidated Statement of Operations found in the accompanying SEC Form 10-K.

CONDENSED BALANCE SHEET

Unaudited and \$ in thousands except per share amounts

	At December 31,	
	2017	2016
Assets:		
Fixed maturities at amortized cost*	\$14,995,101	\$14,188,050
Cash and short-term investments	245,634	148,203
Other investments	638,088	561,827
Deferred acquisition costs*	3,968,882	3,793,439
Goodwill	441,591	441,591
Other assets	1,153,764	1,127,915
Assets related to discontinued operations	68,520	127,532
Total assets*	\$21,511,580	\$20,388,557
Liabilities and shareholders' equity:		
Policy liabilities	\$13,931,831	\$13,286,412
Current and deferred income taxes payable*	899,687	1,377,354
Short-term debt	328,067	264,475
Long-term debt	1,132,201	1,133,165
Other liabilities	489,609	413,760
Liabilities related to discontinued operations	49,854	27,424
Shareholders' equity, excluding ASC 320**	4,680,331	3,885,967
Total liabilities and shareholders' equity	\$21,511,580	\$20,388,557
Actual shares outstanding:		
Basic	114,593	118,031
Diluted	117,696	120,958
Book value (shareholders' equity, excluding ASC 320) per diluted share	\$39.77	\$32.13
Net operating income as a return on average equity, excluding ASC 320	14.3%	14.6%
Average equity, excluding ASC 320	\$4,016,094	\$3,819,969
Debt to capital ratio, excluding ASC 320	23.8%	26.5%
Reconciliation of Torchmark management's view of selected financial items to comparable GAAP measures*:		
Shareholders' equity, excluding ASC 320+	\$4,680,331	\$3,885,967
Effect of ASC 320:		
Increase fixed maturities	1,974,224	1,057,811
Decrease deferred acquisition costs	(10,819)	(10,281)
Increase current and deferred income taxes payable	(412,315)	(366,636)
Shareholders' equity	\$6,231,421	\$4,566,861
Other comparable GAAP measures:		
Fixed maturities at fair value	\$16,969,325	\$15,245,861
Deferred acquisition costs	3,958,063	3,783,158
Total assets	23,474,985	21,436,087
Shareholders' equity	6,231,421	4,566,861
Current and deferred income taxes payable	1,312,002	1,743,990
Book value (shareholders' equity) per diluted share	52.95	37.76
Net income as a return on average equity	28.2%	12.0%
Average equity	\$5,166,815	\$4,595,659
Debt to capital ratio	19.0%	23.4%

*The Condensed Balance Sheet, excluding ASC 320, has been prepared in the manner Torchmark management, industry analysts, rating agencies, and financial institutions use to evaluate the financial position of the Company. It differs from the Consolidated Balance Sheet found in the accompanying SEC Form 10-K.

**ASC 320 includes guidance for treatment of unrealized gains and losses on available-for-sale fixed maturities previously included in FAS 115.

TORCHMARK CORPORATION BOARD OF DIRECTORS



From left to right: David L. Boren, Paul J. Zucconi, Darren M. Rebelez, Steven P. Johnson, Jane M. Buchan, Cheryl D. Alston, Gary L. Coleman, Larry M. Hutchison, Lamar C. Smith, Marilyn A. Alexander, Linda L. Addison, Mary E. Thigpen, Charles E. Adair, Robert W. Ingram, Lloyd W. Newton

Note: Mses. Addison, Alston, and Thigpen were elected to the Board of Directors on February 26, 2018.

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2017

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number: 001-08052



TORCHMARK CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

63-0780404

(I.R.S. Employer
Identification No.)

3700 South Stonebridge Drive, McKinney, TX

(Address of principal executive offices)

75070

(Zip Code)

972-569-4000

(Registrant's telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	CUSIP	Name of each exchange on which registered
Common Stock, \$1.00 par value per share	891027104	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of June 30, 2017, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$8,893,792,769 based on the closing sale price as reported on the New York Stock Exchange.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

<u>Class</u>	<u>Outstanding at February 16, 2018</u>
Common Stock, \$1.00 par value per share	114,081,876 shares

DOCUMENTS INCORPORATED BY REFERENCE

<u>Document</u>	<u>Parts Into Which Incorporated</u>
Proxy Statement for the Annual Meeting of Stockholders to be held April 26, 2018 (Proxy Statement)	Part III

TORCHMARK CORPORATION

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PART I
Item 1. Business

Torchmark Corporation (Torchmark) is an insurance holding company incorporated in Delaware in 1979. Its primary subsidiaries are American Income Life Insurance Company (American Income), Liberty National Life Insurance Company (Liberty National), Globe Life And Accident Insurance Company (Globe), United American Insurance Company (United American), and Family Heritage Life Insurance Company of America (Family Heritage).

Torchmark's website is: www.torchmarkcorp.com. Torchmark makes available free of charge through its website, its annual report on Form 10-K, its quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports as soon as reasonably practicable after they have been electronically filed with or furnished to the Securities and Exchange Commission. Other information included in Torchmark's website is not incorporated into this filing.

The following table presents Torchmark's business by primary marketing distribution method.

	Primary Distribution Method	Company	Products and Target Markets	Distribution
 AMERICAN INCOME LIFE <small>insurance company</small>	American Income Exclusive Agency	American Income Life Insurance Company Waco, Texas	Individual life and supplemental health insurance marketed to working families.	6,880 producing agents in the U.S., Canada, and New Zealand.
 GLOBE LIFE <small>AND ACCIDENT INSURANCE CO.</small>	Globe Life Direct Response	Globe Life And Accident Insurance Company McKinney, Texas	Individual life and supplemental health insurance including juvenile and senior life coverage and Medicare Supplement to middle-income Americans.	Nationwide distribution through direct-to-consumer channels; including direct mail, electronic media and insert media.
 Family Heritage <small>.A Torchmark Company</small>	Family Heritage Exclusive Agency	Family Heritage Life Insurance Company of America Cleveland, Ohio	Supplemental limited-benefit health insurance to middle-income families.	1,076 producing agents in the U.S.
 Liberty National <small>Life Insurance Company</small> <small>Since 1900</small>	Liberty National Exclusive Agency	Liberty National Life Insurance Company McKinney, Texas	Individual life and supplemental health insurance marketed to middle-income families.	2,106 producing agents in the U.S.
 UA United American Insurance Company <small>Since 1947</small>	United American Independent Agency	United American Insurance Company McKinney, Texas	Medicare Supplement coverage to Medicare beneficiaries and, to a lesser extent, supplemental limited-benefit health coverage to people under age 65.	4,192 independent producing agents in the U.S.

Additional information concerning industry segments may be found in *Management's Discussion and Analysis* and in *Note 14—Business Segments* in the *Notes to the Consolidated Financial Statements*.

Insurance

Life Insurance

Torchmark's insurance subsidiaries write a variety of nonparticipating ordinary life insurance products. These include traditional and interest sensitive whole-life insurance, term life insurance, and other life insurance. The following table presents selected information about Torchmark's life products.

	Annualized Premium in Force (Dollar amounts in thousands)					
	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Whole life:						
Traditional	\$ 1,567,077	66	\$ 1,471,054	65	\$ 1,378,290	64
Interest-sensitive	44,286	2	47,358	2	50,808	2
Term	664,558	28	657,797	29	642,599	30
Other	97,178	4	86,527	4	78,801	4
	\$ 2,373,099	100	\$ 2,262,736	100	\$ 2,150,498	100

The distribution methods for life insurance products include direct response, exclusive agents and independent agents. These methods are described in more depth in the Distribution Method chart earlier in this report. The following table presents life annualized premium in force by distribution method.

	Annualized Premium in Force (Dollar amounts in thousands)		
	2017	2016	2015
Globe Life Direct Response	\$ 796,628	\$ 782,222	\$ 757,518
Exclusive agents:			
American Income	1,059,216	966,990	880,021
Liberty National	295,235	288,005	284,597
Independent agents:			
United American	12,121	13,292	14,488
Other	209,899	212,227	213,874
	\$ 2,373,099	\$ 2,262,736	\$ 2,150,498

Health Insurance

Torchmark offers Medicare Supplement and limited-benefit supplemental health insurance products that include primarily critical illness and accident plans. These policies are designed to supplement health coverage that applicants already own. Medicare Supplements are offered to enrollees in the traditional fee-for-service Medicare program. Medicare Supplement plans are standardized by federal regulation and are designed to pay deductibles and co-payments not paid by Medicare.

On July 1, 2016, Torchmark sold its Medicare Part D business to an unaffiliated third party. Torchmark decided to exit its Medicare Part D business due to increasing risks, declining margins, higher drug costs, and increased administrative and compliance costs. Management believes this sale allows the Company to better focus on its core protection life and health insurance businesses. As the historical results for the Medicare Part D business are accounted for as discontinued operations, all business results and relevant forward looking statements of the Company are reported as continuing operations, excluding the Medicare Part D business. For further discussion of the disposition of the Medicare Part D business, see *Note 6—Discontinued Operations*.

The following table presents supplemental health annualized premium in force information for the three years ended December 31, 2017 by product category.

	Annualized Premium in Force (Dollar amounts in thousands)					
	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Medicare Supplement	\$ 495,982	49	\$ 502,691	51	\$ 498,696	51
Limited-benefit plans	522,038	51	495,943	49	474,346	49
	<u>\$ 1,018,020</u>	<u>100</u>	<u>\$ 998,634</u>	<u>100</u>	<u>\$ 973,042</u>	<u>100</u>

The following table presents supplemental health annualized premium in force for the three years ended December 31, 2017 by distribution method.

	Annualized Premium in Force (Dollar amounts in thousands)		
	2017	2016	2015
Direct Response	\$ 76,672	\$ 74,261	\$ 72,423
Exclusive agents:			
Liberty National	205,136	210,260	216,139
American Income	84,775	78,947	74,058
Family Heritage	268,584	249,857	234,120
Independent agents:			
United American	382,853	385,309	376,302
	<u>\$ 1,018,020</u>	<u>\$ 998,634</u>	<u>\$ 973,042</u>

Annuities

Annuity products include single-premium and flexible-premium deferred annuities. Annuities in each of the three years ended December 31, 2017 comprised less than 1% of premium.

Pricing

Premium rates for life and health insurance products are established using assumptions as to future mortality, morbidity, persistency, investment income, expenses, and target profit margins. These assumptions are based on Company experience and projected investment earnings. Revenues for individual life and health insurance products are primarily derived from premium income, and, to a lesser extent, through policy charges to the policyholder account values on annuity products and certain individual life products. Profitability is affected to the extent actual experience deviates from the assumptions made in pricing and to the extent investment income varies from that required for policy reserves.

Collections for annuity products and certain life products are not recognized as revenues, but are added to policyholder account values. Revenues from these products are derived from charges to the account balances for insurance risk and administrative costs. Profits are earned to the extent these revenues exceed actual costs. Profits are also earned from investment income in excess of the amounts credited to policyholder accounts.

Underwriting

The underwriting standards of each Torchmark insurance subsidiary are established by management. Each subsidiary uses information from the application and, in some cases, telephone interviews with applicants, inspection reports, pharmacy data, doctors' statements and/or medical examinations to determine whether a policy should be issued in accordance with the application, with a different rating, with a rider, with reduced coverage or rejected.

Reserves

The life insurance policy reserves reflected in Torchmark's financial statements as future policy benefits are calculated based on accounting principles generally accepted in the United States of America (GAAP). These reserves, with premiums to be received in the future and the interest thereon compounded annually at assumed rates, must be sufficient to cover policy and contract obligations as they mature. Generally, the mortality and persistency assumptions used in the calculations of reserves are based on Company experience. Similar reserves are held on most of the health policies written by Torchmark's insurance subsidiaries, since these policies generally are issued on a guaranteed-renewable basis. The assumptions used in the calculation of Torchmark's reserves are reported in *Note 1—Significant Accounting Policies*. Reserves for annuity products and certain life products consist of the policyholders' account values and are increased by policyholder deposits and interest credited and are decreased by policy charges and benefit payments.

Investments

The nature, quality, and percentage mix of insurance company investments are regulated by state laws. The investments of Torchmark insurance subsidiaries consist predominantly of high-quality, investment-grade securities. Approximately 96% of our invested assets at fair value are fixed maturities at December 31, 2017. (See *Note 4—Investments and Management's Discussion and Analysis*.)

Competition

Torchmark competes with other insurance carriers through policyholder service, price, product design, and sales efforts. While there are insurance companies competing with Torchmark, no individual company dominates any of Torchmark's life or health markets.

Torchmark's health insurance products compete with, in addition to the products of other health insurance carriers, health maintenance organizations, preferred provider organizations, and other health care-related institutions which provide medical benefits based on contractual agreements.

Management believes Torchmark companies operate at lower policy acquisition and administrative expense levels than peer companies. This allows Torchmark to have competitive rates while maintaining higher underwriting margins.

Regulation

Insurance. Insurance companies are subject to regulation and supervision in the states in which they do business. The laws of the various states establish agencies with broad administrative and supervisory powers which include, among other things, granting and revoking licenses to transact business, regulating trade practices, licensing agents, approving policy forms, approving certain premium rates, setting minimum reserve and loss ratio requirements, determining the form and content of required financial statements, and prescribing the type and amount of investments permitted. They are also required to file detailed annual reports with supervisory agencies, and records of their business are subject to examination at any time. Under the rules of the National Association of Insurance Commissioners (NAIC), insurance companies are examined periodically by one or more of the supervisory agencies.

Risk Based Capital. The NAIC requires that a risk based capital formula be applied to all life and health insurers. The risk based capital formula is a threshold formula rather than a target capital formula. It is designed only to identify companies that require regulatory attention and is not to be used to rate or rank companies that are adequately capitalized. All Torchmark insurance subsidiaries are more than adequately capitalized under the risk based capital formula.

Guaranty Assessments. State guaranty laws provide for assessments from insurance companies to be placed into a fund which is used, in the event of failure or insolvency of an insurance company, to fulfill the obligations of that company to its policyholders. The amount which a company is assessed is based on its proportional share of the premium in each state. A significant portion of assessments are recoverable as offsets against state premium taxes. (See *Note 15—Commitments and Contingencies* for current assessment.)

Holding Company. States have enacted legislation requiring registration and periodic reporting by insurance companies domiciled within their respective jurisdictions that control or are controlled by other corporations so as to constitute a holding company system. Torchmark and its subsidiaries have registered as a holding company system pursuant to such legislation in Indiana, Nebraska, Ohio, and New York.

Insurance holding company system statutes and regulations impose various limitations on investments in subsidiaries, and may require prior regulatory approval for material transactions between insurers and affiliates and for the payment of certain dividends and other distributions.

Personnel

At the end of 2017, Torchmark had 3,102 employees.

Item 1A. Risk Factors

Risks Related to Our Business

Product Marketplace and Operational Risks:

The insurance industry is a regulated industry, populated by many public and private companies. We operate in the life and health insurance sectors of the industry, each of which has its own set of risks.

The development and maintenance of our various distribution systems are critical to growth in product sales and profits. Development and retention of producing agents are critical to support sales growth in this market because our insurance sales are primarily made to individuals rather than groups and the face amounts of the life insurance policies sold are typically lower than those of policies sold in higher-income markets. Compensation that is competitive with other career opportunities and motivates producing agents to increase sales is also critical. In Globe Life Direct Response, continuous development of new methods of reaching the consumer and cost efficiency are key. Less than optimum execution of these strategies may result in reduced sales and profits.

Economic conditions may materially adversely affect our business and results of operations. We primarily serve the middle-income market for individual protection life and health insurance and, as a result, we compete directly with alternative uses of a customer's disposable income. If disposable income within this demographic group declines or the use of disposable income becomes more limited as a result of a significant, sustained economic downturn or otherwise, then new sales of our insurance products could become more challenging, and our policyholders may choose to defer or stop payment of insurance premiums altogether. Economic conditions could also impact our investment portfolio as discussed under *Investment Risks* below.

Variations in expected-to-actual rates of mortality, morbidity and persistency could materially negatively affect our results of operations and financial condition. We establish policy reserves to pay future policyholder benefits and claims. These reserves do not represent an exact calculation of liability, but rather are actuarial estimates based on models that include many assumptions and projections which are inherently uncertain. The reserve computations involve the exercise of significant judgment with respect to levels of mortality, morbidity and persistency, as well as the timing of premium and benefit payments. Even though our actuaries continually test expected-to-actual results, actual levels that occur may differ significantly from the levels assumed when premium rates were first set. Accordingly, we cannot determine with precision the ultimate amounts of claims or benefits that we will pay or the timing of such payments. Significant adverse variations from the levels assumed when policy reserves are first set could result in increased policy obligations and negatively affect our profit margins and income.

A ratings downgrade or other negative action by a rating agency could materially affect our business, financial condition and results of operations. Various rating agencies review the financial performance and condition of insurers, including our insurance subsidiaries, and publish their financial strength ratings as indicators of an insurer's ability to meet policyholder and contract holder obligations. These ratings are important to maintaining public confidence in our insurance products. A downgrade or other negative action by a rating agency with respect to the financial strength ratings of our insurance subsidiaries could negatively affect us in many ways, including: limiting or restricting the ability of our insurance subsidiaries to pay dividends to us and adversely affecting our ability to sell insurance products through our independent agencies.

Rating agencies also publish credit ratings for us. Credit ratings are indicators of a debt issuer's ability to meet the terms of debt obligations in a timely manner. These ratings are important to our overall ability to access certain types of capital. Actual or anticipated downgrades in our credit ratings, or an announcement that our ratings are under further review for a downgrade, could potentially have a negative effect on our financial condition and results of operations by limiting our access to capital markets, increasing the cost of debt, or impairing our ability to raise capital to refinance maturing debt obligations, thereby potentially limiting our capacity to support growth at our insurance subsidiaries or making it more difficult to maintain or improve the current financial strength ratings of our insurance subsidiaries.

Ratings reflect only the rating agency's views and are not recommendations to buy, sell or hold our securities. Rating agencies assign ratings based upon several factors. While most of the factors relate to the rated company, some of the factors relate to the views of the rating agency, general economic conditions and circumstances outside the rated company's control. In addition, rating agencies use various models and formulas to assess the strength of a rated company, and from time to time rating agencies have, in their discretion, altered the models. Changes to the models

could impact the rating agencies' judgment of the rating to be assigned to the rated company. There can be no assurance that our current credit ratings will remain in effect for any given period of time or that such ratings will not be lowered, suspended or withdrawn entirely by the rating agencies. We cannot predict what actions the rating agencies may take, or what actions we may take in response to the actions of the rating agencies which could negatively affect our business, financial condition and results of operations.

Life Insurance Marketplace Risk:

Our life products are sold in selected niche markets. We are at risk should any of these markets diminish. We have several life distribution channels that focus on distinct market niches, two of which are labor unions and sales via Globe Life Direct Response solicitation. Deterioration of our relationships with organized labor or adverse changes in the public's receptivity to direct response marketing initiatives could negatively affect our life insurance business.

Health Insurance Marketplace Risks:

The health insurance market is subject to substantial regulatory scrutiny. Regulatory changes could impact our Medicare Supplement and other supplemental health businesses. The nature and timing of any such changes cannot be predicted and could have a material adverse effect on our health insurance business.

Competition in the health insurance market can be significant. Sales of our health insurance products are subject to competition from other health insurance companies and alternative healthcare providers, such as those that provide alternatives to traditional Medicare to seniors. In addition, some insurers may be willing to significantly reduce their profit margins or under price new sales in order to gain market share. We choose not to compete for market share based on these terms. Accordingly, changes in the competitive landscape, including the pricing strategies employed by our competitors, could negatively impact the future sales of our health insurance products.

Obtaining timely and appropriate premium rate increases for certain health insurance policies is critical. A significant percentage of the health insurance premiums that our insurance subsidiaries earn is from Medicare Supplement insurance. Medicare Supplement insurance, including conditions under which the premiums for such policies may be increased, is highly regulated at both the state and federal level. As a result, it is characterized by lower profit margins than life insurance and requires strict administrative discipline and economies of scale for success. Because Medicare Supplement policies are coordinated with the federal Medicare program, which experiences health care inflation every year, annual premium rate increases for the Medicare Supplement policies are typically necessary. Obtaining timely rate increases is of critical importance to our success in this market. Accordingly, the inability of our insurance subsidiaries to obtain approval of premium rate increases in a timely manner from state insurance regulatory authorities in the future could adversely impact their profitability and thus our business, financial condition and results of operations.

Information Security and Technology Risks:

The failure to maintain effective and efficient information systems at the Company could compromise secure data thereby adversely affecting our financial condition and results of operations. Our business operations are highly dependent upon information technology systems to provide efficient and resilient business operations. Malicious actors, employee errors or disasters affecting these information systems could impair our business operations, regulatory compliance and financial condition. To the extent our information systems may be breached by malicious actors, employee malfeasance or technological attacks, an attacker could circumvent security measures in order to access, alter or delete customer or proprietary information from our systems or to render our systems unavailable for business use. Additionally, we may not become aware of sophisticated cyber attacks for some time after they occur, thereby increasing the Company's exposure. We may have to incur significant costs to address or remediate interruptions, threats and vulnerabilities in our information and technology systems and to comply with existing and future regulatory requirements related thereto. These risks are heightened as the frequency and sophistication of cyber-attacks increase.

Employee errors in the handling of our information or technology systems may inadvertently result in unauthorized access to customer or proprietary information, or an inability to use our information technology systems to efficiently support business operations.

Additionally, we anticipate more frequent and sophisticated cyber-attacks along with more impactful regulatory oversight models. In addition, an increasing number of states require that customers be notified of unauthorized access, use or disclosure of their confidential information. Any such breach of confidential information could damage our reputation in the marketplace, deter potential customers from purchasing our products, result in the loss of existing customers, subject us to significant civil and criminal liability, or require us to incur significant technical, legal or other expenses.

In the event of a disaster, such as a natural catastrophe, an industrial accident, a blackout, or a terrorist attack or war, our computer systems may be inaccessible to our employees, agents or customers for a period of time. A disaster or natural catastrophe, an industrial accident, terrorist attack or war may make our information systems unavailable to support business operations for a period of time, which could adversely affect our financial condition and results of operations. Even if our employees are able to report to work, they may be unable to perform their duties for an extended period of time if our data or systems are disabled or destroyed and existing contingency plans cannot function as designed.

Reputational Risk:

Damage to the reputation of Torchmark or its subsidiaries could affect our ability to conduct business. Negative publicity through traditional media, internet, social media and other public forums could damage our reputation and adversely impact our agent recruiting efforts, the ability to market our products and the persistency of our block of inforce policies. As discussed above in *Information Security and Technology Risks*, the Company could be subjected to adverse publicity as a result of a significant security breach.

Investment Risks:

Our investments are subject to market and credit risks. Significant downgrades, delinquencies and defaults in our investment portfolio could potentially result in lower net investment income and increased realized and unrealized investment losses. Our invested assets are subject to the customary risks of defaults, downgrades and changes in market values. Our investment portfolio consists predominately of fixed maturity and short-term investments issued by corporations, where we are exposed to the risk that individual corporate issuers will not have the ability to make required interest or principal payments on an investment. The concentration of these investments in any particular issuer, industry, group of related industries or geographic areas increases this risk. Factors that may affect both market and credit risks include interest rate levels (consisting of both treasury rate and credit spread), financial market performance, disruptions in credit markets, general economic conditions, legislative changes, particular circumstances affecting the businesses or industries of each issuer and other factors beyond our control.

Additionally, as the majority of our investments are longer-term fixed maturities that we typically hold until maturity, significant increases in interest rates or inactive markets associated with market downturns could cause a material temporary decline in the fair value of our fixed investment portfolio, even with regard to performing assets. These declines could cause a material increase in unrealized losses in our investment portfolio. Significant unrealized losses can substantially reduce our capital position and shareholders' equity. It is possible that our investment in certain of these securities with unrealized losses may experience a default event and that a portion or all of that unrealized loss may not be recoverable. In that case, the unrealized loss will be realized, at which point we would take an impairment charge, reducing our net income.

We cannot be assured that any particular issuer, regardless of industry, will be able to make required interest and principal payments on a timely basis or at all. Significant downgrades of issuers could negatively impact our risk-based capital ratios, leading to potential downgrades by our rating agencies, potential reduction in future dividend capacity, and/or higher financing costs at the holding company should additional statutory capital be required.

Changes in interest rates could negatively affect income. Declines in interest rates expose insurance companies to the risk that they will fail to earn the level of interest on investments assumed in pricing products and in setting discount rates used to calculate the net policy liabilities. While we attempt to manage our investments to earn an excess investment income spread, we can give no assurance that a significant and persistent decline in interest rates will not materially affect such spreads. Significant decreases in interest rates could result in calls by issuers of investments, where such features are available to issuers. These calls could result in a decline in our investment income, as reinvestment of the proceeds would likely be at lower rates.

Increases in interest rates could cause the fair value of securities within our bond portfolio to decline. A rise in interest rates could also result in certain policyholders surrendering their annuity policies for cash thereby potentially requiring our insurance subsidiaries to liquidate bonds if other sources of liquidity are not available to meet their obligations. In such a case, realized losses could result from such sales and could adversely affect our statutory income and results of operations.

Liquidity Risks:

Our ability to fund operations is substantially dependent on funds available, primarily dividends, from our insurance subsidiaries. As a holding company with no direct operations, our principal asset is the capital stock of our insurance subsidiaries, which periodically declare and distribute dividends on their capital stock. Moreover, our liquidity, including our ability to pay our operating expenses and to make principal and interest payments on debt securities or other indebtedness owed by us, as well as our ability to pay dividends on our common stock or any preferred stock, depends significantly upon the surplus and earnings of our insurance subsidiaries and the ability of these subsidiaries to pay dividends or to advance or repay funds to us. Other sources of liquidity include a variety of short-term and long-term instruments, including our credit facility, commercial paper, long-term debt, intercompany financing and reinsurance.

The principal sources of our insurance subsidiaries' liquidity are insurance premiums, as well as investment income, maturities, repayments and other cash flow from our investment portfolio. Our insurance subsidiaries are subject to various state statutory and regulatory restrictions applicable to insurance companies that limit the amount of cash dividends, loans and advances that those subsidiaries may pay to us, including laws establishing minimum solvency and liquidity thresholds. For example, in the states where our companies are domiciled, an insurance company generally may pay dividends only out of its unassigned surplus as reflected in its statutory financial statements filed in that state. Additionally, dividends paid by insurance subsidiaries are restricted based on regulations by their states of domicile. Accordingly, impairments in assets or a disruption in our insurance subsidiaries' operations that reduces their capital or cash flow could limit or disallow payment of dividends to us, a principal source of our cash flow.

We can give no assurance that more stringent restrictions will not be adopted from time to time by states in which our insurance subsidiaries are domiciled, which could, under certain circumstances, significantly reduce dividends or other amounts paid to us by our subsidiaries. Although we do not anticipate changes, changes in laws or regulations could constrain the ability of our subsidiaries to pay dividends or to advance or repay funds to us in sufficient amounts and at times necessary to meet our debt obligations and corporate expenses. Additionally, if our insurance subsidiaries were unable to obtain approval of our health premium rate increases in a timely manner from state insurance regulatory authorities, their profitability, and their ability to declare and distribute dividends to us could be negatively impacted. Limitations on the flow of dividends from our subsidiaries could limit our ability to service and repay debt or to pay dividends on our capital stock.

Adverse capital and credit market conditions may significantly affect our ability to meet liquidity needs or access capital, as well as affect our cost of capital. Should interest rates rise in the future, the interest rate on any new debt obligation we may issue could increase and our net income could be reduced. In addition, if the credit and capital markets were to experience significant disruption, uncertainty and instability, these conditions could adversely affect our access to capital. Such market conditions may limit our ability to replace maturing liabilities (in a timely manner or at all) and/or access the capital necessary to grow our business.

In the unlikely event that current sources of liquidity do not satisfy our needs, we may have to seek additional financing or raise capital. The availability and cost of additional financing or capital will depend on a variety of factors such as market conditions, the general availability of credit or capital, the volume of trading activities, the overall availability of credit to the insurance industry and our credit ratings and credit capacity. Additionally, customers, lenders or investors could develop a negative perception of our financial prospects if we were to incur large investment losses or if the level of our business activity were to decrease due to a market downturn. Our access to funds may also be impaired if regulatory authorities or rating agencies take negative actions against us. If our internal sources of liquidity prove to be insufficient, we may not be able to successfully obtain additional financing on favorable terms or at all. As such, we may be forced to delay raising capital, issue shorter term securities than we prefer or bear an unattractive cost of capital which could decrease our profitability and significantly reduce our financial flexibility. As a result, our results of operations, financial condition and cash flows could be materially negatively affected.

Regulatory Risks:

Our businesses are heavily regulated and changes in regulation may reduce our profitability and growth.

Insurance companies, including our insurance subsidiaries, are subject to extensive supervision and regulation in the states in which they do business. The primary purpose of this supervision and regulation is the protection of our policyholders, not our investors. State agencies have broad administrative power over numerous aspects of our business, including premium rates and other terms and conditions that we can include in the insurance policies offered by our insurance subsidiaries, marketing practices, advertising, licensing of agents, policy forms, capital adequacy, solvency, reserves and permitted investments. Also, regulatory authorities have relatively broad discretion to grant, renew or initiate procedures to revoke licenses or approvals. The insurance laws, regulations and policies currently affecting Torchmark and its insurance subsidiaries may change at any time, possibly having an adverse effect on our business. Should these regulatory changes occur, we may be unable to maintain all required licenses and approvals, and our business may not fully comply with the wide variety of applicable laws and regulations or the relevant authority's interpretation of such laws and regulations, which may change from time to time. If we do not have the requisite licenses and approvals or do not comply with applicable regulatory requirements, the insurance regulatory authorities could preclude or temporarily suspend us from carrying on some or all of our activities and/or impose substantial fines.

We cannot predict the timing or substance of any future regulatory initiatives. In recent years, there has been increased scrutiny of insurance companies, including our insurance subsidiaries, by insurance regulatory authorities, which has included more extensive examinations and more detailed review of disclosure documents. These regulatory authorities may bring regulatory or other legal actions against us if, in their view, our practices, or those of our agents or employees, are improper. Such actions could result in substantial fines, penalties and/or prohibitions or restrictions on our business activities, and could have a material adverse effect on our business, results of operations or financial condition. Additionally, changes in the overall legal or regulatory environment may cause us to change our views regarding the actions that we need to take from a legal or regulatory risk management perspective, thus necessitating changes to our practices that may, in some cases, limit our ability to grow, impact regulatory capital requirements, or otherwise negatively impact our profitability.

Currently, the U.S. federal government does not directly regulate the business of insurance. However, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 established a Federal Insurance Office (FIO), charged with monitoring systemic risk exposure in the insurance industry, and a Financial Stability Oversight Council (FSOC), which serves to identify and respond to risks and emerging threats to U.S. financial systems. A Center for Consumer Information and Insurance Oversight (CCIO), established under the Department of Health and Human Services, is charged with overseeing implementation of the Affordable Care Act (ACA). The creation of these insurance regulatory offices may indicate that the federal government intends to play a larger role in the direct oversight or regulation of the insurance industry. We cannot predict what impact, if any, the ongoing operations of the FIO, FSOC and CCIO, as well as any other proposals or executive action for federal oversight or regulation of insurance could have on our business, results of operations or financial condition.

Changes in U.S. federal income tax law could increase our tax costs or negatively impact our insurance subsidiaries' capital.

Changes to the Internal Revenue Code, administrative rulings, or court decisions affecting the insurance industry, including the products insurers offer, could increase our effective tax rate and lower our net income, adversely impact our insurance subsidiaries' capital, or limit the ability of our insurance subsidiaries to sell certain of their products.

Changes in accounting standards issued by accounting standard-setting bodies may affect our financial statements, reduce our reported profitability and change the timing of profit recognition.

Our financial statements are subject to the application of GAAP and accounting practices as promulgated by the National Association of Insurance Commissioners' statutory accounting practices (NAIC SAP), which principles are periodically revised and/or expanded. Accordingly, from time to time we are required to adopt new or revised accounting standards or guidance issued by recognized authoritative bodies. It is possible that future accounting standards that we are required to adopt could change the current accounting treatment that we apply to our consolidated financial statements and that such changes could have a material adverse effect on our financial condition and results of operations. Further, standard setters have a full agenda of unissued topics under review at any given time, many of which have the potential to negatively impact our profitability.

Non-compliance with restrictions on customer and consumer privacy and information security, including taking steps to ensure that our business associates who obtain access to sensitive customer and consumer information maintain its confidentiality, could materially adversely affect our reputation and business operations. The collection, maintenance, use, disclosure and disposal of individually identifiable data by our insurance subsidiaries are regulated at the international, federal and state levels. These laws and rules are subject to change by legislation or administrative or judicial interpretation. Various state laws address the use and disclosure of individually identifiable health data to the extent they are more restrictive than those contained in the privacy and security provisions in the federal Gramm-Leach-Bliley Act of 1999 (GLBA), the Health Information Technology for Economic and Clinical Health Act (HITECH), and in the Health Insurance Portability and Accountability Act of 1996 (HIPAA). HIPAA also requires that we impose privacy and security requirements on our business associates (as that term is defined in the HIPAA regulations). Noncompliance with any privacy laws or any security breach involving the misappropriation, loss or other unauthorized disclosure of sensitive or confidential information, whether by us or by one of our business associates, could have a material adverse effect on our business, reputation and results of operations and could include material fines and penalties, various forms of damages, consent orders regarding our privacy and security practices, adverse actions against our licenses to do business and injunctive relief.

Litigation Risk:

Litigation could result in substantial judgments against us or our subsidiaries. We are, and in the future may be, subject to litigation in the ordinary course of business. Some of these proceedings have been brought on behalf of various alleged classes of complainants, and, in certain of these matters, the plaintiffs are seeking large and/or indeterminate amounts, including punitive or exemplary damages. Members of our management and legal teams review litigation on a quarterly and annual basis. However, the outcome of any such litigation cannot be predicted with certainty. A number of civil jury verdicts have been returned against insurers in the jurisdictions in which our insurance subsidiaries do business involving the insurers' sales practices, alleged agent misconduct, failure to properly supervise agents and other matters. These lawsuits have resulted in the award of substantial judgments against insurers that are disproportionate to the actual damages, including material amounts of punitive damages. In some states in which we operate, juries have substantial discretion in awarding punitive damages. This discretion creates the potential for unpredictable material adverse judgments in any given punitive damages suit.

Our pending and future litigation could adversely affect us because of the costs of defending these cases, the costs of settlement or judgments against us, or changes in our operations that could result from litigation. Substantial legal liability in these or future legal actions could also have a material adverse financial effect or cause significant harm to our reputation, which, in turn, could materially harm our business and our business prospects.

Actual or alleged misclassification of independent contractors at our insurance subsidiaries could result in adverse legal, tax or financial consequences. A significant portion of our sales agents are independent contractors. Although we believe we have properly classified such individuals, a risk nevertheless exists that a court, the IRS or other authority will take the position that those sales agents are employees. The laws and regulations that govern the status and classification of workers are subject to change and differing interpretations, which we cannot predict.

If there is an adverse determination regarding the classification of some or all of the independent contractors at our insurance subsidiaries by a court or governmental agency, we could incur significant costs with respect to payroll tax liabilities, employee benefits, wage payments, fines, judgments and/or legal settlements, any of which could have a material adverse effect on our business, financial condition and results of operations. In addition, any resulting reclassification could necessitate significant changes in our affected insurance subsidiaries' business models.

Catastrophic Event Risk:

Our business is subject to the risk of the occurrence of catastrophic events. Our insurance policies are issued to and held by a large number of policyholders throughout the United States in relatively low-face amounts. Accordingly, it is unlikely that a large portion of our policyholder base would be affected by a single natural disaster. However, our insurance operations could be exposed to the risk of catastrophic mortality or morbidity caused by events such as a pandemic, hurricane, earthquake, or man-made catastrophes, including acts of terrorism or war, which may produce significant claims in larger areas, especially those that are heavily populated. Claims resulting from natural or man-made catastrophic events could cause substantial volatility in our financial results for any fiscal quarter or year and could materially reduce our profitability or harm our financial condition.

Item 1B. Unresolved Staff Comments

As of December 31, 2017, Torchmark had no unresolved staff comments.

Item 2. Properties

Torchmark, through its subsidiaries, owns or leases buildings that are used in the normal course of business. Torchmark owns and occupies a 300,000 square foot facility in McKinney, Texas. This facility is Torchmark's corporate headquarters and also houses the operations of a subsidiary, United American, as well as many operations of other subsidiaries. In addition, United American leases 5,000 square feet of space in Omaha, Nebraska and, through a subsidiary, leases 3,230 square feet of office space in Syracuse, New York.

Liberty National, also in McKinney, Texas, leases a 24,000 square foot facility in Hoover, Alabama (a Birmingham suburb). An 8,000 square foot facility is leased for storage in Pelham, Alabama.

Globe leases 34,000 square feet of office area in the Cotter Tower building located in downtown Oklahoma City, Oklahoma. Globe also leases 11,000 square feet at a nearby facility used for storage. Globe Marketing Services, a subsidiary of Globe, owns a 133,000 square foot facility in Oklahoma City which houses the Globe Life Direct Response operation.

American Income owns and occupies two buildings located in Waco, Texas: 70,000 square foot building for corporate operations and a 43,000 square foot printing facility. American Income also leases 10,800 square feet in a building across the street from the main office building. American Income also leases office space throughout the United States to support its marketing operations.

Family Heritage owns 50% of a partnership that owns a 66,000 square foot building in Broadview Heights, Ohio (a suburb of Cleveland), serving as Family Heritage's headquarters. The partnership also leases a portion of the building to unrelated tenants.

Item 3. Legal Proceedings

Torchmark and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims involving tax matters, alleged breaches of contract, torts, including bad faith and fraud claims based on alleged wrongful or fraudulent acts of agents of Torchmark's subsidiaries, employment discrimination, and miscellaneous other causes of action. Based upon information presently available, and in light of legal and other factual defenses available to Torchmark and its subsidiaries, management does not believe that such litigation will have a material adverse effect on Torchmark's financial condition, future operating results or liquidity; however, assessing the eventual outcome of litigation necessarily involves forward-looking speculation as to judgments to be made by judges, juries and appellate courts in the future. This bespeaks caution, particularly in states with reputations for high punitive damage verdicts. Torchmark's management recognizes that large punitive damage awards bearing little or no relation to actual damages continue to be awarded by juries in jurisdictions in which Torchmark and its subsidiaries have substantial business, creating the potential for unpredictable material adverse judgments in any given punitive damage suit.

See further discussion of litigation and unclaimed property audits in *Note 15—Commitments and Contingencies*.

Item 4. Mine Safety Disclosures.

Not Applicable.

PART II

**Item 5. Market for Registrant’s Common Equity,
Related Stockholder Matters and Issuer Purchases of Equity Securities**

Market Price of and Dividends on the Registrant’s Common Equity and Related Stockholder Matters

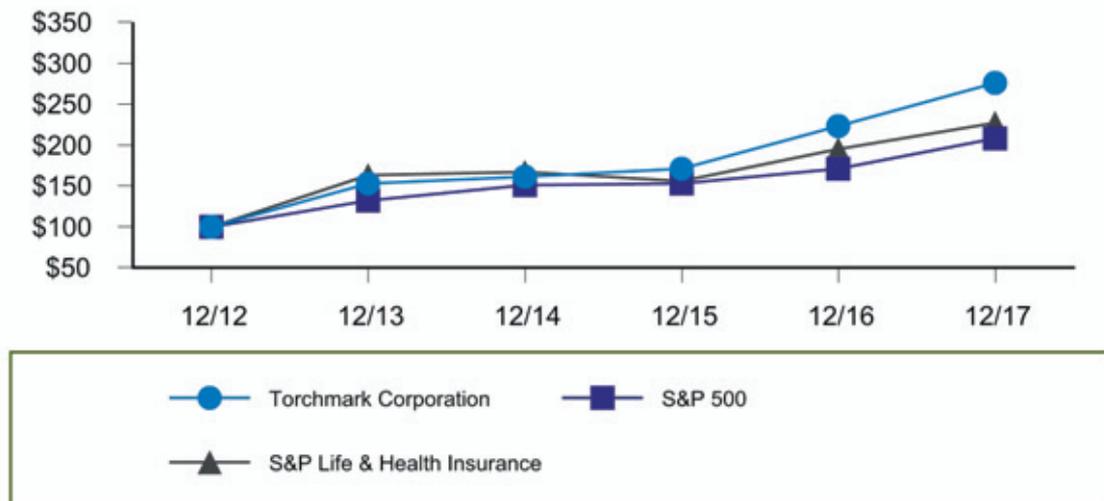
The principal market in which Torchmark’s common stock is traded is the New York Stock Exchange. There were 2,662 shareholders of record on December 31, 2017, excluding shareholder accounts held in nominee form. The market prices and cash dividends paid by calendar quarter for the past two years are presented in the following table.

<u>Quarter</u>	2017 Market Price		Dividends Per Share
	High	Low	
1	\$ 78.71	\$ 73.00	\$ 0.140
2	77.77	74.11	0.150
3	80.09	74.68	0.150
4	91.16	80.32	0.150
Year-end closing price \$	90.71		

<u>Quarter</u>	2016 Market Price		Dividends Per Share
	High	Low	
1	\$ 57.01	\$ 48.58	\$ 0.135
2	62.39	52.83	0.140
3	65.21	60.38	0.140
4	74.83	63.17	0.140
Year-end closing price \$	73.76		

The line graph shown below compares Torchmark’s cumulative total return on its common stock with the cumulative total returns of the Standard and Poor’s 500 Stock Index (S&P 500) and the Standard and Poor’s Life & Health Insurance Index (S&P Life & Health Insurance). Torchmark is one of the companies whose stock is included within both the S&P 500 and the S&P Life & Health Insurance Index.

**Comparison of 5 Year Cumulative Total Return*
Among Torchmark Corporation, the S&P 500 Index, and the S&P Life & Health
Insurance Index**



*100 invested on 12/31/12 in stock or index, including reinvestment of dividends. Fiscal year ended December 31st.
(Copyright © 2018 Standard & Poor's, a division of S&P Global. All rights reserved.)

Purchases of Certain Equity Securities by the Issuer and Others for the Fourth Quarter 2017

<u>Period</u>	<u>(a) Total Number of Shares Purchased</u>	<u>(b) Average Price Paid Per Share</u>	<u>(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</u>	<u>(d) Maximum Number of Shares (or Approximate Dollar Amount) that May Yet Be Purchased Under the Plans or Programs</u>
October 1-31, 2017	260,690	\$ 82.44	260,690	—
November 1-30, 2017 ..	593,200	85.22	593,200	—
December 1-31, 2017 ..	439,315	89.91	439,315	—

On August 7, 2017, Torchmark's Board reaffirmed its continued authorization of the Company's stock repurchase program in amounts and with timing that management, in consultation with the Board, determined to be in the best interest of the Company. The program has no defined expiration date or maximum number of shares to be purchased.

Item 6. Selected Financial Data

The following information should be read in conjunction with Torchmark's Consolidated Financial Statements and related notes reported elsewhere in this Form 10-K:

(Dollar amounts in thousands except per share and percentage data)

Year ended December 31,	2017	2016	2015	2014	2013
Premium revenue:					
Life	\$ 2,306,547	\$ 2,189,333	\$ 2,073,065	\$ 1,966,300	\$ 1,885,332
Health	976,373	947,663	925,520	869,440	863,818
Other	15	38	135	400	532
Total	3,282,935	3,137,034	2,998,720	2,836,140	2,749,682
Net investment income	847,885	806,903	773,951	758,286	734,650
Realized investment gains (losses)	23,611	(10,683)	(8,791)	23,548	7,990
Total revenue	4,155,573	3,934,629	3,766,065	3,620,095	3,494,253
Income from continuing operations, net of tax	1,458,263	539,590	516,293	528,074	507,205
Income from discontinued operations, net of tax	(3,769)	10,189	10,807	14,865	21,267
Net income ⁽¹⁾	1,454,494	549,779	527,100	542,939	528,472
Per common share:					
Basic earnings:					
Income from continuing operations	12.53	4.50	4.13	4.04	3.68
Income from discontinued operations	(0.03)	0.08	0.08	0.11	0.16
Net income	12.50	4.58	4.21	4.15	3.84
Diluted earnings:					
Income from continuing operations	12.26	4.41	4.07	3.98	3.63
Income from discontinued operations	(0.04)	0.08	0.09	0.11	0.16
Net income ⁽¹⁾	12.22	4.49	4.16	4.09	3.79
Cash dividends declared	0.60	0.56	0.54	0.51	0.45
Cash dividends paid	0.59	0.56	0.53	0.49	0.44
Basic weighted average shares outstanding	116,343	120,001	125,095	130,722	137,647
Diluted weighted average shares outstanding	118,983	122,368	126,757	132,640	139,564
As of December 31,	2017	2016	2015	2014	2013
Cash and invested assets	\$17,853,047	\$15,955,891	\$14,405,073	\$15,058,996	\$13,456,944
Total assets	23,474,985	21,436,087	19,853,213	20,272,259	18,217,757
Short-term debt	328,067	264,475	490,129	238,398	229,070
Long-term debt	1,132,201	1,133,165	743,733	992,130	990,865
Shareholders' equity ⁽¹⁾	6,231,421	4,566,861	4,055,552	4,697,466	3,776,342
Per diluted common share ⁽¹⁾	52.95	37.76	32.71	36.19	27.66
Effect of fixed maturity revaluation on diluted equity per common share ⁽²⁾	13.18	5.63	2.62	8.28	1.81
Annualized premium in force:					
Life	2,373,099	2,262,736	2,150,498	2,044,545	1,955,401
Health	1,018,020	998,634	973,042	947,323	887,444
Total	3,391,119	3,261,370	3,123,540	2,991,868	2,842,845
Basic shares outstanding	114,593	118,031	122,370	127,930	134,252
Diluted shares outstanding	117,696	120,958	123,996	129,812	136,537

(1) On December 22, 2017, the Tax Cuts and Jobs Act was enacted into law which revises corporate income tax rates from 35% to 21%, among other modifications. See further discussion of the tax reform implications in the *Results of Operations*. Excluding the effects of tax reform, net income, net income per diluted common share, shareholders' equity and shareholders' equity per diluted common share would have been \$581 million, \$4.88, \$5.36 billion and \$45.52, respectively.

(2) There is accounting guidance (ASC 320-10-35-1, *Investments- Debt and Equity Securities*) requiring available-for-sale fixed maturities to be recorded at fair value each period. The effect of this rule on diluted equity per share reflects the amount added or (deducted) under this rule to produce GAAP Shareholders' equity per share. See discussion under the caption *Capital Resources* in *Management's Discussion and Analysis* in this report concerning the effect this rule has on Torchmark's equity.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the *Selected Financial Data* and Torchmark's *Consolidated Financial Statements* and *Notes* thereto appearing elsewhere in this report.

RESULTS OF OPERATIONS

How Torchmark Views Its Operations: Torchmark is the holding company for a group of insurance companies which market primarily individual life, and supplemental health insurance to middle income households throughout the United States. We view our operations by segments, which are the insurance product lines of life, health, and annuities, and the investment segment that supports the product lines. Segments are aligned based on their common characteristics, comparability of the profit margins, and management techniques used to operate each segment.

Insurance Product Line Segments. As fully explained in *Note 14—Business Segments*, the insurance product line segments involve the marketing, underwriting, and the administration of policies. Each product line is further segmented by the various distribution units that market the insurance policies. Each distribution unit operates in a niche market offering insurance products designed for that particular market. Whether analyzing profitability of a segment as a whole, or the individual distribution units within the segment, the measure of profitability used by management is the underwriting margin, which is:

Premium revenue
Less:
Policy obligations
Policy acquisition costs and commissions

Investment Segment. The investment segment involves the management of our capital resources, including investments and the management of corporate debt and liquidity. Our measure of profitability for the investment segment is excess investment income, which is:

Net investment income
Less:
Required interest on net policy liabilities
Financing costs

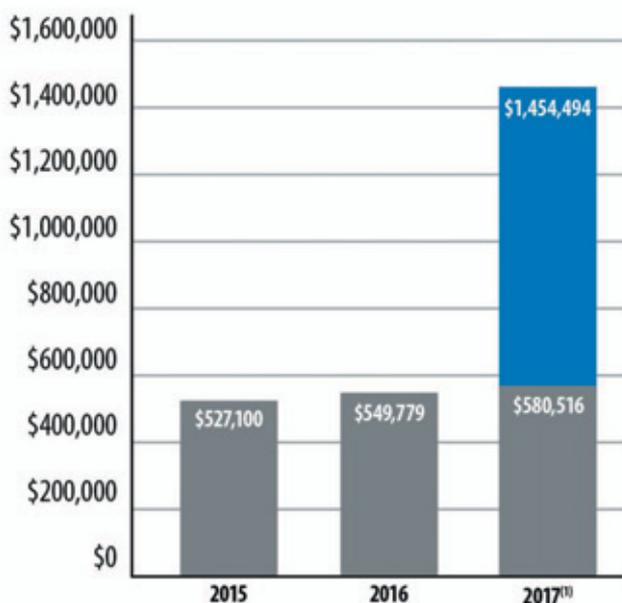
The tables in *Note 14—Business Segments* in the *Notes to the Consolidated Financial Statements* reconcile Torchmark's revenues and expenses by segment to its major income statement line items for each of the years in the three-year period ended December 31, 2017.

Current Year Highlights:

- Net income as a return on equity (ROE) was 28.2%⁽¹⁾ and net operating income as a ROE, excluding net unrealized gains on the fixed maturity portfolio was 14.3%⁽¹⁾.
- Total premium increased by 5% over the prior year. Life premium also increased by 5% for the year from \$2.2 billion to \$2.3 billion. Life underwriting margin also increased 5% from \$574 million in 2016 to \$604 million in 2017.
- Net investment income increased 5% over the prior year. In addition, excess investment income, a measure used by management as explained below, increased by 7% over the prior year.
- During 2017, the Company repurchased 4.1 million shares at a total cost of \$325 million for an average share price of \$78.67.

The following represents net income and net operating income from continuing operations for the 3 years ended December 31, 2017.

NET INCOME (\$ in thousands)



NET OPERATING INCOME FROM CONTINUING OPERATIONS (\$ in thousands)



- (1) As further discussed below regarding Tax Legislation, excluding the tax reform adjustment, net income as a ROE and net operating income as a ROE would have been 11.7% and 14.4%, respectively. In 2017, the Company recorded a one-time adjustment of \$874 million impacting net income. As the impact of the Tax Legislation was treated as a non-operating event, it was excluded from net operating income.

Net income as a ROE and net operating income as a ROE, excluding net unrealized gains on the fixed maturity portfolio in 2016 were 12.0% and 14.6%, respectively and 11.9% and 14.5%, respectively in 2015. Net operating income as a ROE, excluding net unrealized gains on the fixed maturity portfolio is considered a non-GAAP measure. Management utilizes this measure to view the business without the effect of the unrealized gains or losses which are primarily attributable to fluctuation in interest rates on the available-for-sale portfolio.

Summary of Operations: Net income was \$1.5 billion in 2017, compared with \$550 million in 2016. This sharp increase was due to an \$874 million increase to net income, primarily relating to a reduction of deferred income tax liabilities resulting from enactment of the Tax Cuts and Jobs Act of 2017 (Tax Legislation). See further discussion below. Net income also increased in 2016 from \$527 million in 2015. On a diluted per common share basis, 2017 net income rose

172% to \$12.22 after an 8% increase in 2016, again largely related to implementation of the Tax Legislation. Without the impact of the Tax Legislation, net income per diluted common share would have been \$4.88. Net income per diluted common share in 2016 rose to \$4.49 from \$4.16 in 2015. The per share results have exceeded the growth in dollar amounts due to our share repurchase program. Each year's per share net income was affected by realized investment gains (losses), which were \$0.15, \$(0.06), and \$(0.05), in 2017, 2016 and 2015, respectively. More information concerning realized investment gains and losses can be found under the caption *Realized Gains and Losses* in this report.

Net operating income from continuing operations rose each year over the prior year from \$523 million in 2015 to \$549 million in 2016 to \$574 million in 2017. Net operating income is the consolidated total of segment profits after tax and as such is considered a non-GAAP measure. Net income is the most directly comparable GAAP measure. See *Note 14—Business Segments* for a discussion of the usefulness and purpose of this measure. We do not consider realized gains and losses to be a component of our core insurance operations or operating segments. Additionally, net income was affected by certain significant and unusual non-operating items in each of the years 2015 through 2017. We do not view these items as components of core operating results because they are not indicative of past performance or future prospects of the insurance operations. We remove items such as these that relate to prior periods or are non-operating items when evaluating the results of current operations, and therefore exclude such matters from our segment analysis for current periods.

Tax Cuts and Jobs Act of 2017: On December 22, 2017, the Tax Legislation was enacted which changed existing tax law, including a reduction of the corporate income tax rate from 35% to 21% effective January 1, 2018. The Company recorded \$877 million of tax benefits in net income as a result of re-measuring its deferred tax liabilities using the lower corporate tax rate as of the date of enactment. Based on the analysis of the Tax Legislation, the Company was able to determine that this amount is a reasonable estimate of the impact of the Tax Legislation in accordance with SEC Staff Accounting Bulletin No. 118. However, the Company will continue to analyze relevant information to complete the accounting for income taxes which may result in an adjustment to income tax expense in 2018. The accounting is expected to be complete when the 2017 U.S. corporate income tax returns are filed later in 2018. In addition, the Company early adopted ASU 2018-02, *Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*, and recorded a \$252 million reclassification from *Accumulated Other Comprehensive Income* to *Retained Earnings* to eliminate the stranded tax effects associated with the tax rate change, primarily relating to the unrealized gains and losses on the available-for-sale fixed maturity portfolio. More information concerning income taxes is provided in *Note 8—Income Taxes*.

There will be substantial long-term benefits from the Tax Legislation due to the taxation of future profits at the new 21% tax rate. Looking forward, we are anticipating the effective tax rate on our net operating income before stock compensation expense to decrease and be in the range of 19% to 20%. Despite the lower expected tax rate for financial reporting purposes, in the short and intermediate term, we do not anticipate a significant reduction in our current tax expense, as benefits of the lower tax rate will be virtually offset by several provisions included in the Tax Legislation that increase the Company's current taxable income.

The below table illustrates the impact of the tax reform adjustment on certain balances.

	Prior to tax adjustment	Tax reform adjustment	GAAP balance
Current and deferred income taxes payable	\$ 2,189,402	\$ (877,400)	\$ 1,312,002
Accumulated other comprehensive income (loss)	1,171,874	252,400	1,424,274
Retained earnings	4,181,208	625,000	4,806,208
Shareholders' equity	5,357,443	873,978	6,231,421
Income before income taxes	834,028	(3,380)	830,648
Income tax benefit (expense)	(249,743)	877,358	627,615
Net income	580,516	873,978	1,454,494
Total diluted net income per common share	4.88	7.34	12.22

Torchmark's operations on a segment-by-segment basis are discussed in depth under the appropriate captions following in this report.

Analysis of Profitability by Segment
(Dollar amounts in thousands)

	2017	2016	2015	2017 Change	%	2016 Change	%
Life insurance underwriting margin	\$ 604,337	\$ 573,762	\$ 569,402	\$ 30,575	5	\$ 4,360	1
Health insurance underwriting margin	219,508	210,056	204,377	9,452	4	5,679	3
Annuity underwriting margin	10,562	9,394	4,568	1,168	12	4,826	106
Excess investment income	239,363	224,031	219,504	15,332	7	4,527	2
Other insurance:							
Other income	1,270	1,534	2,379	(264)	(17)	(845)	(36)
Administrative expense	(210,590)	(196,598)	(186,191)	(13,992)	7	(10,407)	6
Corporate and other	(43,285)	(34,913)	(37,667)	(8,372)	24	2,754	(7)
Pre-tax total	821,165	787,266	776,372	33,899	4	10,894	1
Applicable taxes	(247,484)	(237,906)	(253,459)	(9,578)	4	15,553	(6)
Net operating income from continuing operations	573,681	549,360	522,913	24,321	4	26,447	5
Discontinued operations—Part D, net of tax...	—	9,033	10,807	(9,033)	(100)	(1,774)	(16)
Net operating income	573,681	558,393	533,720	15,288	3	24,673	5
Reconciling items, net of tax:							
Realized gains (losses)—investments	17,590	(6,944)	(5,714)	24,534		(1,230)	
Part D adjustments—discontinued operations	(3,769)	1,156	—	(4,925)		1,156	
Guaranty fund assessments	(1,171)	—	—	(1,171)		—	
Administrative settlements	(5,628)	(2,467)	(906)	(3,161)		(1,561)	
Non-operating fees	(187)	(359)	—	172		(359)	
Tax reform adjustment	873,978	—	—	873,978		—	
Net income	<u>\$ 1,454,494</u>	<u>\$ 549,779</u>	<u>\$ 527,100</u>	<u>\$904,715</u>	165	<u>\$ 22,679</u>	4

The life insurance segment is our strongest segment and is the largest contributor to earnings in each year presented. This segment contributed \$31 million in 2017 and \$4 million in 2016 to the growth in our underwriting margin. Also contributing to growth in income in both years was our health insurance segment, which provided \$9 million of additional margin in 2017 and \$6 million in 2016.

Excess investment income, the measure of profitability of our investment segment, increased 7% to \$239 million from the prior year amount of \$224 million. In 2016, excess investment income increased 2%. Investment yields continue to be pressured by investing at yields lower than the yield on dispositions and the average yield on the portfolio.

Total revenues rose 6% in 2017 to \$4.2 billion, or \$221 million over the prior year total of \$3.9 billion. Life premium rose 5% or \$117 million in 2017 to \$2.3 billion. Life premium increased \$116 million in 2016 to \$2.2 billion. Net investment income rose \$41 million or 5% in 2017, and rose 4% or \$33 million in 2016. Health premium increased 3% to \$976 million in 2017 and contributed \$29 million to 2017 revenue growth, after having gained 2% to \$948 million in 2016. Health premium contributed \$22 million to 2016 revenue growth.

Life insurance premium and underwriting margins have grown in each of the last three years ended December 31, 2017. The increase in life premium was driven by sales growth and improvements in persistency. While premium and underwriting margins grew, margin as a percent of premium remained flat in 2017 at 26%, after decreasing from 27% to 26% from 2015 to 2016. Net life sales increased in 2017 to \$416 million. Net life sales were flat between 2015 and 2016. The life insurance segment is discussed further in this report under the caption *Life Insurance*.

Health insurance premium income increased 3% to \$976 million in 2017. Health net sales rose 9% to \$158 million during 2017 due to both individual and group sales. Group sales vary significantly from period to period due to the impact of large groups that are sold from time-to-time. First-year collected health premium fell 3% to \$136 million from the prior year total of \$140 million as a result of higher net sales in Medicare Supplement in the fourth quarter of 2015 that positively affected the 2016 first-year collected premium. Health margins as a percentage of premium were flat at 22%, with underwriting income increasing to \$220 million for 2017 due to the growth in premium income. Underwriting income was \$210 million in 2016 compared with \$204 million in 2015. The health insurance segment is discussed further in this report under the caption *Health Insurance*.

We do not currently market annuities. See the caption *Annuities* for discussion of the Annuity segment.

Excess investment income, is based on three major components: net investment income, required interest on net policy liabilities (interest applicable to insurance products), and financing costs. In 2017, net investment income rose 5%, compared with 4% in 2016. At the same time, our investment portfolio grew 6% in 2017 and 2016, on an amortized cost basis. In recent years, the percentage growth in net investment income has been less than the growth in the overall investment portfolio due primarily to new investments being made at yield rates lower than the yield rates on dispositions and the average yield on the portfolio. The growth rate of net investment income is impacted at times by a lag between the time when proceeds from maturities and dispositions are received and when the proceeds are reinvested, during which the funds are held in cash. In addition, Torchmark's share repurchase program (described later under this caption) has diverted cash that could have otherwise been used to acquire investments and increase net investment income. The growth in the investment portfolio has been augmented in 2017 and 2016 due to the receipt of certain receivables that had accumulated under our Medicare Part D business.

The interest required on net policy liabilities is deducted from net investment income, and generally grows in conjunction with the net policy liabilities that are supported by the invested assets. The lower new-money yields resulting from the low interest rate environment noted above have compressed excess investment income as required interest has continued to grow at approximately the same rate that net policy liabilities have grown. Financing costs, which consist of the interest required for debt service on our long and short-term debt, are also deducted from net investment income. Financing costs in 2017 increased 1% to \$85 million from \$83 million in 2016. The additional interest expense resulted primarily from an increase in the cost of our short-term borrowings and, in lesser part, from the issuance of our new 5.275% Junior Subordinated Debt security thirty-six days before the repayment of our 5.875% Junior Subordinated Debt security.

Insurance administrative expenses were up 7.1% in 2017 when compared with the prior year period, and increased to 6.4% as a percentage of premium from 6.3% in 2016 and 6.2% in 2015. The increase in administrative expenses is primarily due to an increase in other employee costs and investments in information technology. Corporate and Other expenses were up primarily due to an increase in stock-based compensation expense, reflecting Torchmark's higher share price as compared with the same period a year ago, and recognition of a one-time increase in stock-based compensation expense due to the Tax Legislation.

Share Purchases

Torchmark has in place an ongoing share repurchase program which began in 1986. With no specified authorization amount, we determine the amount of repurchases based on the amount of the excess cash flow at the Parent Company, general market conditions, and other alternative uses. The majority of these purchases are made from excess cash flow. Excess cash flow at the Parent Company is primarily comprised of dividends received from the insurance subsidiaries less interest expense paid on its debt, dividends paid to Torchmark shareholders, and other limited operating activities. Additionally, when stock options are exercised, proceeds from these exercises and the resulting tax benefit are used to repurchase additional shares on the open market to minimize dilution as a result of the option exercises. The Board of Directors has authorized the Company's share repurchase program in amounts and with timing that management, in consultation with the Board, determines to be in the best interest of the Company and its shareholders. The following chart summarizes share purchase activity for each of the last three years.

Analysis of Share Purchases (Amounts in thousands)

<u>Purchases</u>	<u>2017</u>		<u>2016</u>		<u>2015</u>	
	<u>Shares</u>	<u>Amount</u>	<u>Shares</u>	<u>Amount</u>	<u>Shares</u>	<u>Amount</u>
Share repurchase program	4,126	\$ 324,622	5,208	\$ 311,332	6,292	\$ 358,552
Option proceeds	1,103	88,367	1,487	93,452	1,049	59,974
Total	<u>5,229</u>	<u>\$ 412,989</u>	<u>6,695</u>	<u>\$ 404,784</u>	<u>7,341</u>	<u>\$ 418,526</u>

Throughout the remainder of this discussion, share purchases refer only to those made from excess cash flow at the Parent Company.

A discussion of each of Torchmark's segments follows. The following discussions are presented in the manner we view our operations, as described in *Note 14—Business Segments*.

Life Insurance

Life insurance is our largest insurance segment, with 2017 life premium representing 70% of total premium. Life underwriting income before other income and administrative expense represented 72% of the total in 2017. Additionally, investments supporting the reserves for life products produce the majority of excess investment income attributable to the investment segment.

We use three statistical measures as indicators of premium growth and sales over the near term: "annualized premium in force," "net sales," and "first-year collected premium."

- Annualized premium in force is defined as the premium income that would be received over the following twelve months at any given date on all active policies if those policies remain in force throughout the twelve-month period. Annualized premium in force is an indicator of potential growth in premium revenue.
- Net sales is annualized premium issued (Gross premium that would be received during the policies' first year in force and assuming that none of the policies lapsed or terminated.), net of cancellations in the first thirty days after issue, except in the case of Globe Life Direct Response where net sales is annualized premium issued at the time the first full premium is paid after any introductory offer period has expired. We believe that net sales is a better indicator of the rate of premium growth as compared to annualized premium issued.
- First-year collected premium is defined as the premium collected during the reporting period for all policies in their first policy year. First-year collected premium takes lapses into account in the first year when lapses are more likely to occur, and thus is a useful indicator of how much new premium is expected to be added to premium income in the future.

The following table presents the summary of results of life insurance. Further discussion of the results by distribution channel is included below.

LIFE INSURANCE
Summary of Results
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Premium	Amount	% of Premium	Amount	% of Premium
Premium and policy charges.....	\$2,306,547	100	\$2,189,333	100	\$2,073,065	100
Policy obligations	1,549,602	67	1,475,477	67	1,374,608	67
Required interest on reserves	(607,007)	(26)	(577,827)	(26)	(552,298)	(27)
Net policy obligations	942,595	41	897,650	41	822,310	40
Commissions, premium taxes, and non-deferred acquisition expenses	177,111	8	164,476	8	154,811	8
Amortization of acquisition costs	582,504	25	553,445	25	526,542	25
Total expense	1,702,210	74	1,615,571	74	1,503,663	73
Insurance underwriting margin before other income and administrative expenses	\$ 604,337	26	\$ 573,762	26	\$ 569,402	27

Life insurance premium rose 5% to \$2.3 billion in 2017 after having increased 6% in 2016 to \$2.2 billion. Life insurance products are marketed through several distribution channels. Premium income by distribution channel for each of the last three years is as follows:

LIFE INSURANCE
Premium by Distribution Channel
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
American Income Exclusive Agency	\$ 999,279	43	\$ 913,355	42	\$ 830,903	40
Globe Life Direct Response	812,907	35	782,765	36	746,693	36
Liberty National Exclusive Agency	274,635	12	270,476	12	271,113	13
Other Agencies	219,726	10	222,737	10	224,356	11
	\$2,306,547	100	\$2,189,333	100	\$2,073,065	100

Annualized life premium in force was \$2.37 billion at December 31, 2017, an increase of 4.9% over \$2.26 billion a year earlier. Annualized life premium in force was \$2.15 billion at December 31, 2015.

The following table shows net sales information for each of the last three years by distribution channel.

LIFE INSURANCE
Net Sales by Distribution Channel
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
American Income Exclusive Agency	\$ 223,259	54	\$ 209,856	51	\$ 198,046	48
Globe Life Direct Response	135,704	33	150,267	36	164,348	40
Liberty National Exclusive Agency	46,886	11	40,159	10	35,782	9
Other Agencies	10,233	2	11,673	3	13,705	3
	<u>\$ 416,082</u>	<u>100</u>	<u>\$ 411,955</u>	<u>100</u>	<u>\$ 411,881</u>	<u>100</u>

The table below discloses first-year collected life premium by distribution channel.

LIFE INSURANCE
First-Year Collected Premium by Distribution Channel
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
American Income Exclusive Agency	\$ 182,538	58	\$ 173,573	56	\$ 156,206	52
Globe Life Direct Response	92,057	29	98,496	31	106,417	35
Liberty National Exclusive Agency	33,191	10	29,103	9	27,554	9
Other Agencies	9,633	3	11,458	4	12,036	4
	<u>\$ 317,419</u>	<u>100</u>	<u>\$ 312,630</u>	<u>100</u>	<u>\$ 302,213</u>	<u>100</u>

The **American Income Exclusive Agency** has historically marketed primarily to members of labor unions. While labor unions are still the core market for this agency, American Income has diversified in recent years by focusing heavily on other affinity groups, third party internet vendor leads, and referrals to help ensure sustainable growth. This agency is Torchmark's largest contributor to life premium of any distribution channel at 43% of Torchmark's 2017 total. This group produced premium income of \$999 million, an increase of 9% over the prior year total of \$913 million, after having risen 10% in 2016. First-year collected premium was \$183 million compared to \$174 million in 2016, an increase of 5%. First-year collected premium rose 11% in 2016. Net sales increased 6% to \$223 million in 2017 over the 2016 total of \$210 million. Net sales increased 6% in 2016 over the 2015 total of \$198 million. Sales growth in our captive agencies is generally dependent on growth in the size of the agency force. The American Income Agency's average agent count rose 4% to 6,962 in 2017. The average producing agent count is based on the actual count at the end of each week during the period.

The American Income Exclusive Agency continues to focus on growing and strengthening middle management to support sustainable growth of the agency force. To accomplish this, the agency places an emphasis on agent training programs and financial incentives that appropriately reward agents at all levels for helping develop and train its agents, including more home-office and webinar training programs. These programs are designed to provide each agent, from new recruits to top level managers, coaching and instruction specifically designed for their level of experience and responsibility. We have made considerable investments in information technology in support of the agency, including the launching of a lead mapping and management tool to the agency force. We anticipate this tool will help the Agency enhance agent productivity and agent retention.

The **Globe Life Direct Response** unit offers adult and juvenile life insurance through a variety of direct-to-consumer marketing approaches, which include direct mailings, insert media, and electronic media. These different approaches support and complement one another in the unit's efforts to reach the consumer. The Globe Life Direct Response channel's growth has been fueled by constant innovation. In recent years, electronic media production has grown rapidly as management has aggressively increased marketing activities related to internet and mobile technology, and has focused on driving traffic to the inbound call center. We continually introduce new initiatives in this unit in an attempt to increase response rates.

While the juvenile market is an important source of sales, it also is a vehicle to reach the parents and grandparents of juvenile policyholders, who are more likely to respond favorably to a Globe Life Direct Response solicitation for life coverage on themselves than is the general adult population. Also, both juvenile policyholders and their parents are low acquisition-cost targets for sales of additional coverage over time.

Globe Life Direct Response's life premium income rose 4% to \$813 million, representing 35% of Torchmark's total life premium during 2017. Life premium in this channel increased 5% in 2016 to \$783 million over the 2015 total of \$747 million. Net sales of \$136 million for this group decreased 10% from \$150 million in 2016, after a 9% decrease in 2016 due to operational changes designed to maximize underwriting margin dollars. We expect sales to decline, consistent with this recent trend, through 2018. First-year collected premium decreased 7% to \$92 million in 2017 after having decreased 7% in 2016.

The **Liberty National Exclusive Agency** markets individual and group life insurance to middle-income customers. Life premium income for this agency was \$275 million in 2017, an increase of 2% from \$270 million in 2016. Life premium income in 2015 totaled \$271 million. Net sales increased 17% during 2017 to \$47 million over the 2016 total of \$40 million. Net sales in 2016 increased 12%. The continued increases in net sales reflect changes in structure of the agency that were put in place several years ago. Middle management has also grown within the agency which will help continue this growth. First-year collected premium increased 14% to \$33 million during 2017 and increased 6% in 2016 to \$29 million.

The Liberty average producing agent count increased from 1,715 in 2016 to 2,017 in 2017. We continue to execute our long term plan to grow this agency through expansion from small-town markets in the southeast to more densely populated areas with larger pools of potential agent recruits and customers. Expansion of this agency's presence into more heavily populated, less-penetrated areas will help create long term agency growth. Additionally, the agency's prospecting training program has helped to improve the ability of agents to develop new work site marketing business.

The **Other Agencies** distribution channels offering life insurance include the Military Agency, the UA Independent Agency (which predominantly writes health insurance), and various smaller distribution channels. The Other Agencies contributed \$220 million of life premium income, or 10% of Torchmark's total in 2017, but contributed only 2% of net sales for the year.

Health Insurance

Health insurance sold by Torchmark includes primarily Medicare Supplement insurance, critical illness coverage, accident coverage, and other limited-benefit supplemental health products. In this analysis, all health coverage plans other than Medicare Supplement are classified as limited-benefit plans.

Health premium accounted for 30% of our total premium in 2017, while the health underwriting margin accounted for 26% of total underwriting margin, reflective of the lower underwriting margin as a percent of premium for health compared with life insurance. As noted under the caption *Life Insurance*, we have emphasized life insurance sales relative to health, due to life's superior profitability and its greater contribution to excess investment income.

The following table presents the summary of results for health insurance.

HEALTH INSURANCE Summary of Results (Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Premium	Amount	% of Premium	Amount	% of Premium
Premium	\$ 976,373	100	\$ 947,663	100	\$ 925,520	100
Policy obligations	628,640	65	612,725	65	602,610	65
Required interest on reserves.....	(77,792)	(8)	(73,382)	(8)	(69,057)	(7)
Net policy obligations.....	550,848	57	539,343	57	533,553	58
Commissions, premium taxes, and non-deferred acquisition expenses	86,044	9	84,819	9	81,489	9
Amortization of acquisition costs.....	119,973	12	113,445	12	106,101	11
Total expense	756,865	78	737,607	78	721,143	78
Insurance underwriting margin before other income and administrative expense	\$ 219,508	22	\$ 210,056	22	\$ 204,377	22

Health premium increased 3% from \$948 million in 2016 to \$976 million in 2017. Health underwriting margin increased 4% from \$210 million in 2016 to \$220 million in 2017. Further discussion is included below by distribution channels.

Premium income by distribution channel for each of the last three years is as follows:

HEALTH INSURANCE
Premium by Distribution Channel
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
United American Independent Agency						
Limited-benefit plans	\$ 11,438		\$ 12,704		\$ 15,260	
Medicare Supplement	352,690		342,311		330,070	
	364,128	37	355,015	38	345,330	37
Family Heritage Exclusive Agency						
Limited-benefit plans	253,534		236,075		221,091	
Medicare Supplement	—		—		—	
	253,534	26	236,075	25	221,091	24
Liberty National Exclusive Agency						
Limited-benefit plans	144,128		142,026		142,130	
Medicare Supplement	52,079		59,772		67,020	
	196,207	20	201,798	21	209,150	23
American Income Exclusive Agency						
Limited-benefit plans	88,776		84,064		79,984	
Medicare Supplement	260		318		355	
	89,036	9	84,382	9	80,339	9
Direct Response						
Limited-benefit plans	545		552		869	
Medicare Supplement	72,923		69,841		68,741	
	73,468	8	70,393	7	69,610	7
Total Premium						
Limited-benefit plans	498,421	51	475,421	50	459,334	50
Medicare Supplement	477,952	49	472,242	50	466,186	50
	\$976,373	100	\$947,663	100	\$925,520	100

We market supplemental health insurance products through a number of distribution channels. The following table presents net sales by distribution channel for the last three years.

HEALTH INSURANCE
Net Sales by Distribution Channel
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
United American Independent Agency						
Limited-benefit plans	\$ 500		\$ 558		\$ 734	
Medicare Supplement	60,670		55,451		70,891	
	<u>61,170</u>	39	<u>56,009</u>	39	<u>71,625</u>	46
Family Heritage Exclusive Agency						
Limited-benefit plans	56,534		51,349		50,266	
Medicare Supplement	—		—		—	
	<u>56,534</u>	36	<u>51,349</u>	35	<u>50,266</u>	32
Liberty National Exclusive Agency						
Limited-benefit plans	20,407		19,513		18,021	
Medicare Supplement	—		9		41	
	<u>20,407</u>	13	<u>19,522</u>	13	<u>18,062</u>	12
American Income Exclusive Agency						
Limited-benefit plans	13,943		12,666		11,501	
Medicare Supplement	—		—		—	
	<u>13,943</u>	9	<u>12,666</u>	9	<u>11,501</u>	7
Direct Response						
Limited-benefit plans	—		—		—	
Medicare Supplement	5,582		5,560		5,003	
	<u>5,582</u>	3	<u>5,560</u>	4	<u>5,003</u>	3
Total Net Sales						
Limited-benefit plans	91,384	58	84,086	58	80,522	51
Medicare Supplement	66,252	42	61,020	42	75,935	49
	<u>\$157,636</u>	<u>100</u>	<u>\$145,106</u>	<u>100</u>	<u>\$156,457</u>	<u>100</u>

The following table discloses first-year collected health premium by distribution channel.

HEALTH INSURANCE
First-Year Collected Premium by Distribution Channel
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
United American Independent Agency						
Limited-benefit plans	\$ 458		\$ 547		\$ 660	
Medicare Supplement	54,393		64,848		76,575	
	<u>54,851</u>	40	<u>65,395</u>	47	<u>77,235</u>	49
Family Heritage Exclusive Agency						
Limited-benefit plans	44,535		40,822		39,196	
Medicare Supplement	—		—		—	
	<u>44,535</u>	33	<u>40,822</u>	29	<u>39,196</u>	25
Liberty National Exclusive Agency						
Limited-benefit plans	16,425		16,103		14,690	
Medicare Supplement	2		6		168	
	<u>16,427</u>	12	<u>16,109</u>	11	<u>14,858</u>	9
American Income Exclusive Agency						
Limited-benefit plans	14,673		13,710		12,041	
Medicare Supplement	—		—		—	
	<u>14,673</u>	11	<u>13,710</u>	10	<u>12,041</u>	8
Direct Response						
Limited-benefit plans	—		—		(2)	
Medicare Supplement	5,657		4,457		13,843	
	<u>5,657</u>	4	<u>4,457</u>	3	<u>13,841</u>	9
Total First-Year Collected Premium						
Limited-benefit plans	76,091	56	71,182	51	66,585	42
Medicare Supplement	60,052	44	69,311	49	90,586	58
	<u>\$136,143</u>	<u>100</u>	<u>\$140,493</u>	<u>100</u>	<u>\$157,171</u>	<u>100</u>

The **UA Independent Agency** consists of independent agencies appointed with Torchmark who may also sell for other companies. The UA Independent Agency was Torchmark's largest health agency in terms of health premium income. In 2017, premium income was \$364 million, representing 37% of Torchmark's total health premium. Net sales were \$61 million, or 39% of Torchmark's health sales. This agency is also Torchmark's largest producer of Medicare Supplement insurance, with Medicare Supplement premium income of \$353 million. The UA Independent Agency represents 74% of all Torchmark Medicare Supplement premium and 92% of Medicare Supplement net sales. Medicare Supplement premium in this agency rose 3% in 2017. Total health premium increased 3% in 2017 and 2016. Medicare Supplement net sales increased 9% in 2017 from the prior year due to increases in individual and group sales. Group Medicare Supplement sales have historically fluctuated from period to period.

The **Family Heritage Exclusive Agency** primarily markets limited-benefit supplemental health insurance in non-urban areas. Most of their policies include a cash-back feature, such as a return of premium whereby any excess of premiums over claims paid is returned to the policyholder at the end of a specified period stated within the insurance policy. Management expects to grow this agency through geographic expansion and continuing incorporation of Torchmark's recruiting systems. The Family Heritage Agency contributed \$57 million in net sales in 2017, compared with \$51 million in 2016 and \$50 million in 2015. Health premium income was \$254 million in 2017, representing 26% of Torchmark's

health premium. This compared with \$236 million or 25% of health premium in 2016 and \$221 million or 24% in 2015. The average producing agent count was 995 for the year ended December 31, 2017, compared with 923 for the same period in 2016, an increase of 8%.

The **Liberty National Exclusive Agency** represented 20% of all Torchmark health premium income at \$196 million in 2017. The Liberty Agency markets limited-benefit supplemental health products consisting primarily of critical illness insurance. Much of Liberty's health business is now generated through work site marketing targeting small businesses of 10 to 25 employees. In 2017, health premium income declined 3% after declining 4% during 2016. Liberty's health premium decline has been due primarily to its declining Medicare Supplement block. Liberty's first-year collected premium increased 2% to \$16 million in 2017 compared with an increase of 8% in 2016, reflecting the steady increase in net sales of limited-benefit plans in the agency.

Other distribution. Certain of our other distribution channels market health products, although their main emphasis is on life insurance. On a combined basis, they accounted for 17% of health premium in 2017 and 16% in 2016. The American Income Exclusive Agency primarily markets accident plans. The Direct Response group markets primarily Medicare Supplements to employer or union-sponsored groups. Direct Response added \$6 million of Medicare Supplement net sales in 2017 and 2016 and \$5 million in 2015.

In 2016 and 2015, the Affordable Care Act (ACA) imposed an annual fee to health insurance issuers offering commercial health insurance as well as another fee for premium stabilization. These fees totaled \$621 thousand and \$1.2 million in 2016 and 2015, respectively. There were no fees for 2017.

Annuities. Our fixed annuity balances at the end of 2017 and 2016 were \$1.25 billion and \$1.29 billion, respectively. Underwriting income was \$10.6 million, \$9.4 million, and \$4.6 million for the three years ended December 31, 2017, respectively.

While the fixed annuity account balance has been declining slightly year over year, underwriting income has increased each year over the prior year. The significant increase in underwriting income in 2016 was primarily due to a slowdown in amortization as assumptions were adjusted to reflect longer retention of the annuity block than previously estimated as a result of the continuing low interest rate environment. Policy charges have actually declined slightly in each successive year. The majority of policy charges consist of surrender charges which are based on a function of account size and time lapsed since deposit. A considerable portion of fixed annuity profitability is derived from the spread of investment income exceeding contractual interest requirements, which can result in negative net policy obligations. We do not currently market annuity products, favoring instead protection-oriented life and health insurance products. Therefore, we do not expect that annuities will be a significant portion of our business or marketing strategy going forward.

Administrative expenses. Operating expenses are included in the Corporate and Other segment and are classified into two categories: insurance administrative expenses and expenses of the Parent Company. The following table is an analysis of operating expenses for the three years ended December 31, 2017.

Operating Expenses Selected Information
(Dollar amounts in thousands)

	2017		2016		2015	
	Amount	% of Premium	Amount	% of Premium	Amount	% of Premium
Insurance administrative expenses:						
Salaries	\$ 96,185	2.9	\$ 91,415	2.9	\$ 87,262	2.9
Non-salary employee costs	33,539	1.0	29,852	1.0	30,683	1.0
Information technology costs	26,048	0.8	23,303	0.7	17,307	0.6
Other administrative expense	46,066	1.4	43,727	1.4	43,694	1.4
Legal expense—insurance	8,752	0.3	8,301	0.3	7,245	0.3
Total insurance administrative expenses ...	210,590	6.4	196,598	6.3	186,191	6.2
Parent company expense	9,631		8,587		9,003	
Stock-based compensation expense	37,034		26,326		28,664	
Non-operating fees	—		553		—	
Total operating expenses, per <i>Consolidated Statements of Operations</i> ..	\$257,255		\$232,064		\$223,858	

Insurance administrative expenses:			
Increase (decrease) over prior year	7.1%	5.6%	6.5%
Total operating expenses:			
Increase (decrease) over prior year	10.9%	3.7%	2.9%

Insurance administrative expenses were up 7.1% in 2017 when compared with the prior year after increasing 5.6% during 2016. As a percentage of total premium, insurance administrative expenses increased to 6.4% in 2017 from 6.3% in 2016 and 6.2% 2015. Total operating expenses increased 10.9% in 2017, after increasing 3.7% in 2016. The increase in other employee costs was due primarily to higher pension expense driven by lower interest rates.

The increase in information technology costs was due to investments that will enhance our customer experience, expand our data analytics capabilities, modernize our systems in order to improve our ability to react quickly to future changes, and bolster our information security programs.

The increase in stock-based compensation expense was primarily due to higher expense associated with equity awards, reflecting Torchmark's higher share price and higher stock option values as compared with the same period a year ago. The increase also reflects a one-time increase in stock-based compensation expense due to the effects of the Tax Legislation as previously discussed.

Investments. We manage our capital resources including investments, debt, and cash flow through the investment segment. Excess investment income represents the profit margin attributable to investment operations. It is the measure that we use to evaluate the performance of the investment segment as described in *Note 14—Business Segments*. It is defined as net investment income less both the required interest attributable to net policy liabilities and the interest cost associated with capital funding or “financing costs.”

We also view excess investment income per diluted common share as an important and useful measure to evaluate the performance of the investment segment. It is defined as excess investment income divided by the total diluted weighted average shares outstanding, representing the contribution by the investment segment to the consolidated earnings per share of the Company. Since implementing our share repurchase program in 1986, we have used \$7.1 billion of excess cash flow at the Parent Company to repurchase Torchmark shares after determining that the repurchases provided a greater return than other investment alternatives. If we had not used this excess cash to repurchase shares, but had instead invested it in interest-bearing assets, we would have earned more investment income and had more shares outstanding. In order to put all capital resource uses on a comparable basis, we believe that excess investment income per diluted share is an appropriate measure of the investment segment.

Excess Investment Income. The following table summarizes Torchmark’s investment income and excess investment income.

Analysis of Excess Investment Income
(Dollar amounts in thousands except for per share data)

	2017	2016	2015
Net investment income	\$ 847,885	\$ 806,903	\$ 773,951
Interest on net insurance policy liabilities:			
Interest on reserves	(734,370)	(702,340)	(674,650)
Interest on deferred acquisition costs	210,380	202,813	196,845
Net required interest	(523,990)	(499,527)	(477,805)
Financing costs	(84,532)	(83,345)	(76,642)
Excess investment income	<u>\$ 239,363</u>	<u>\$ 224,031</u>	<u>\$ 219,504</u>
Excess investment income per diluted share	<u>\$ 2.01</u>	<u>\$ 1.83</u>	<u>\$ 1.73</u>
Mean invested assets (at amortized cost)	\$15,376,781	\$14,461,502	\$13,697,129
Average net insurance policy liabilities ⁽¹⁾	9,359,780	8,945,850	8,574,699
Average debt and preferred securities (at amortized cost).....	1,458,706	1,379,933	1,343,663

(1) Net of deferred acquisition costs, excluding the associated unrealized gains and losses thereon.

Excess investment income increased \$15 million or 7% during 2017 after increasing 2% during 2016. The rate of growth was higher in 2017 than in 2016, in part, because excess investment income during 2016 was negatively impacted by an increase in financing costs attributable to the early refinancing of our 6.375% Senior Notes as is discussed below in the discussion of our financing costs. In addition, the growth rate in 2017 was positively impacted by the investment of positive cash flows relating to the collection in 2016 and 2017 of various receivables that had accumulated in prior years in the Medicare Part D business.

Excess investment income per diluted common share increased 10% during 2017 after increasing 6% during 2016. Excess investment income per diluted common share generally increases at a faster pace than excess investment income because the number of diluted shares outstanding generally decreases from year to year as a result of our share repurchase program.

The largest component of excess investment income is net investment income, which increased at a compound annual growth rate of 4% during the last three years. Growth in net investment income has been negatively impacted in recent years by the declining interest rate environment during which time we have invested new money and reinvested the

proceeds from bonds that matured or were called or otherwise disposed of at yield rates less than what we earned on these bonds before their maturity or disposition. We currently expect that the average annual turnover rate of fixed maturity assets during the next five years will not exceed 1% to 3% of the portfolio, and will not have a significant negative impact on the growth of net investment income. Presented in the following chart is the growth in net investment income and the growth in mean invested assets.

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Growth in net investment income	5.1%	4.3%	2.1%
Growth in mean invested assets (at amortized cost)	6.3%	5.6%	3.2%

Should interest rates rise, especially long-term rates, Torchmark's net investment income would benefit due to higher interest rates on new purchases. While such a rise in interest rates could adversely affect the fair value of the fixed maturities portfolio, we could withstand an increase in interest rates of approximately 100 to 105 basis points before the net unrealized gains on our fixed maturity portfolio as of December 31, 2017 would be eliminated. Should interest rates increase further than that, we would not be concerned with potential interest rate driven unrealized losses in our fixed maturity portfolio because we have the intent and, more importantly, the ability, to hold our fixed maturities to maturity.

Required interest on net insurance policy liabilities reduces net investment income as it is the amount of net investment income considered by management necessary to "fund" the required interest included in the insurance segments. As such, it is removed from the investment segment and applied to the insurance segments to offset the effect of the required interest from the insurance segments. As discussed in *Note 14-Business Segments*, management believes this provides a more meaningful analysis of the investment and insurance segments. Required interest is based on the actuarial interest assumptions used in discounting the benefit reserve liability and the amortization of deferred acquisition costs for our insurance policies in force. The great majority of our life and health insurance policies are fixed interest-rate protection policies, not investment products, and are accounted for under current accounting guidance for long-duration insurance products which mandates that interest rate assumptions for a particular block of business be "locked in" for the life of that block of business. Each calendar year, we set the discount rate to be used to calculate the benefit reserve liability and the amortization of the deferred acquisition cost asset for all insurance policies issued that year. That rate is based on the new money yields that we expect to earn on cash flow received in the future from policies of that issue year, and cannot be changed. The discount rate used for policies issued in the current year has no impact on the in force policies issued in prior years as the rates of all prior issue years are also locked in. As such, the overall discount rate for the entire in force block is a weighted average of the discount rates being used from all issue years. Changes in the overall weighted-average discount rate over time are caused by changes in the mix of the reserves and the deferred acquisition cost asset by issue year on the entire block of in force business. Business issued in the current year has very little impact on the overall weighted-average discount rate due to the size of our in force business.

Since actuarial discount rates are locked in for life on essentially all of our business, benefit reserves and deferred acquisition costs are not affected by interest rate fluctuations unless a loss recognition event occurs. Due to the strength of our underwriting margins and the current positive spread between the yield on our investment portfolio and the weighted-average discount rate of our in force block, we do not expect an extended low-interest-rate environment to cause a loss recognition event.

Information about interest on net policy liabilities is shown in the following table.

Required Interest on Net Insurance Policy Liabilities
(Dollar amounts in thousands)

	Required Interest	Average Net Insurance Policy Liabilities	Average Discount Rate
2017			
Life and Health	\$ 468,038	\$ 8,099,319	5.78%
Annuity	55,952	1,260,461	4.44
Total	<u>\$ 523,990</u>	<u>\$ 9,359,780</u>	5.60
Increase in 2017	4.90%	4.63%	
2016			
Life and Health	\$ 442,021	\$ 7,658,639	5.77%
Annuity	57,506	1,287,211	4.47
Total	<u>\$ 499,527</u>	<u>\$ 8,945,850</u>	5.58
Increase in 2016	4.55%	4.33%	
2015			
Life and Health	\$ 418,432	\$ 7,256,732	5.77%
Annuity	59,373	1,317,967	4.50
Total	<u>\$ 477,805</u>	<u>\$ 8,574,699</u>	5.57
Increase in 2015	4.37%	4.06%	

Excess investment income is also impacted by financing costs. Financing costs for the investment segment primarily consist of interest on our various debt instruments and are deducted from excess investment income. The table below presents the components of financing costs and reconciles interest expense per the *Consolidated Statements of Operations*.

Analysis of Financing Costs
(Dollar amounts in thousands)

	2017	2016	2015
Interest on funded debt	\$ 74,115	\$ 75,988	\$ 71,180
Interest on term loan	2,336	993	—
Interest on short-term debt	8,076	6,360	5,457
Other	5	4	5
Financing costs	<u>\$ 84,532</u>	<u>\$ 83,345</u>	<u>\$ 76,642</u>

Financing costs increased \$1 million or 1% from 2016 to 2017. In 2017, interest on short-term debt increased because of the increase in the weighted-average interest rate on such debt. Financing costs also increased \$7 million or 9% from 2015 to 2016 due primarily to the additional interest expense on our funded debt associated with the issuance of a 6.125% Junior Subordinated Debt security seventy days before the maturity and repayment of the 6.375% Senior Notes. More information on our debt transactions are disclosed in the *Financial Condition* section of this report and in *Note 11—Debt*.

Realized Gains and Losses. Our life and health insurance companies collect premium income from policyholders for the eventual payment of policyholder benefits, sometimes paid many years or even decades in the future. Because benefits are expected to be paid in future periods, premium receipts in excess of current expenses are invested to provide for these obligations. For this reason, we hold a significant investment portfolio as a part of our core insurance operations. This portfolio consists primarily of high-quality fixed maturities containing an adequate yield to provide for the cost of carrying these long-term insurance product obligations. As a result, fixed maturities are generally held for

long periods to support the liabilities. Expected yields on these investments are taken into account when setting insurance premium rates and product profitability expectations.

Despite our intent to hold fixed maturity investments for a long period of time, investments are occasionally sold or called, resulting in a realized gain or loss. These gains and losses generally occur only incidentally, usually as the result of bonds sold because of deterioration in investment quality of issuers or calls by the issuers. Investment losses are also caused by write downs due to impairments. We do not engage in trading investments for profit. Therefore, gains or losses which occur in protecting the portfolio or its yield, or which result from events that are beyond our control, are only secondary to our core insurance operations of providing insurance coverage to policyholders.

Realized gains and losses can be significant in relation to the earnings from core insurance operations, and as a result, can have a material positive or negative impact on net income. The significant fluctuations caused by gains and losses can cause period-to-period trends of net income that are not indicative of historical core operating results or predictive of the future trends of core operations. Accordingly, they have no bearing on core insurance operations or segment results as we view operations. For these reasons, and in line with industry practice, we remove the effects of realized gains and losses when evaluating overall insurance operating results.

The following table summarizes our tax-effected realized gains (losses) by component for each of the years in the three-year period ended December 31, 2017.

Analysis of Realized Gains (Losses), Net of Tax
(Dollar amounts in thousands, except for per share data)

	Year Ended December 31,					
	2017		2016		2015	
	Amount	Per Share	Amount	Per Share	Amount	Per Share
Fixed maturities:						
Sales	\$ 2,587	\$ 0.02	\$ (17,209)	\$ (0.14)	\$ (10,813)	\$ (0.09)
Called or tendered	20,292	0.17	10,290	0.08	4,652	0.04
Write-downs	(159)	—	—	—	—	—
Loss on redemption of debt	(2,627)	(0.02)	—	—	—	—
Other	(2,503)	(0.02)	(25)	—	447	—
Total	<u>\$ 17,590</u>	<u>\$ 0.15</u>	<u>\$ (6,944)</u>	<u>\$ (0.06)</u>	<u>\$ (5,714)</u>	<u>\$ (0.05)</u>

As described in *Note 4—Investments* under the caption *Other-than-temporary impairments*, the Company recorded \$245 thousand (\$159 thousand, net of tax) in security write-downs. We did not incur any write downs in our fixed maturity portfolio as a result of other-than-temporary impairment for the years 2015 and 2016.

Investment Acquisitions. Torchmark’s investment policy calls for investing in fixed maturities that are investment grade and meet our quality and yield objectives. We generally prefer to invest in securities with longer maturities because they more closely match the long-term nature of our policy liabilities. We believe this strategy is appropriate because our cash flows are generally stable and predictable. If longer-term securities that meet our quality and yield objectives are not available, we do not relax our quality objectives, but instead, consider investing in shorter term or lower yielding securities, taking into consideration the slope of the yield curve and other factors.

During calendar years 2015 through 2017, Torchmark invested almost exclusively in fixed maturity securities, primarily in corporate bonds with longer-term maturities. The following table summarizes selected information for fixed maturity purchases for the last three years. The effective annual yield shown is the yield calculated to the potential termination date that produces the lowest yield, commonly referred to as the “worst call date.” For non-callable bonds, the worst-call date is always the maturity date. For callable bonds, the worst-call date is the call date that produces the lowest yield, typically the first call date.

Fixed Maturity Acquisitions Selected Information

(Dollar amounts in thousands)

	Year Ended December 31,		
	2017	2016	2015
Cost of acquisitions ⁽¹⁾ :			
Investment-grade corporate securities	\$ 1,308,567	\$ 1,505,135	\$ 1,026,520
Taxable municipal securities	—	13,023	29,092
Other investment-grade securities	6,042	14,727	15,296
Total fixed maturity acquisitions	<u>\$ 1,314,609</u>	<u>\$ 1,532,885</u>	<u>\$ 1,070,908</u>
Effective annual yield (one year compounded) ⁽²⁾	4.67%	4.67%	4.79%
Average life (in years, to next call)	23.0	24.6	27.2
Average life (in years to maturity)	24.0	25.4	27.9
Average rating	BBB+	BBB+	BBB+

(1) Includes unsettled trades of \$3 million for 2016.

(2) Tax-equivalent basis, where the yield on tax-exempt securities is adjusted to produce a yield equivalent to the pretax yield on taxable securities.

We prefer to invest primarily in bonds that are not callable (on other than a make-whole basis) prior to maturity, but we periodically invest some funds in callable bonds when the incremental yield available on such bonds warrants doing so. For investments in callable bonds, the actual life of the investment will depend on whether the issuer calls the investment prior to the maturity date. Given our investments in callable bonds, the actual average life of our investments cannot be known at the time of the investment. Absent sales, however, the average life will not be less than the average life to next call and will not exceed the average life to maturity. Data for both of these average life measures is provided in the above chart.

From 2015 through 2017, acquisitions consisted of securities spanning a diversified range of issuers, industry sectors, and geographical regions. All of the acquired securities were investment grade. In addition to the fixed maturity acquisitions, Torchmark invested \$55 million in other long-term investments in 2017 compared with \$20 million in 2016 and \$32 million in 2015.

New cash flow available for investment has been primarily provided through our insurance operations and interest received on existing investments. The amount of cash available for investment in 2016 was greater than 2015 due in part to the collection of various receivables from our Medicare Part D business. In some years, a significant amount of new investments can be derived from proceeds from dispositions including issuer calls. While calls increase funds available for investment, as noted earlier in this discussion, they can also have a negative impact on investment income if the proceeds from the calls are reinvested in bonds that have lower yields than those of the bonds that were called. Issuer calls were \$371 million in 2017, \$182 million in 2016, and \$178 million in 2015.

Portfolio Composition. The composition of the investment portfolio at book value on December 31, 2017 and 2016 was as follows:

Invested Assets

(Dollar amounts in thousands)

	2017		2016	
	Amount	% of Total	Amount	% of Total
Fixed maturities (at amortized cost)	\$ 14,995,101	95	\$ 14,188,050	96
Policy loans	529,529	3	507,975	3
Other long-term investments ⁽¹⁾	107,953	1	53,355	—
Short-term investments	127,071	1	72,040	1
Total	<u>\$ 15,759,654</u>	<u>100</u>	<u>\$ 14,821,420</u>	<u>100</u>

(1) Includes equities available for sale at cost.

Approximately 95% of our investments at book value are in a diversified fixed maturity portfolio. Policy loans, which are secured by policy cash values, make up 3% of our investments. We also have insignificant investments in equity securities and other long-term investments. Because fixed maturities represent such a significant portion of our investment portfolio, the remainder of the discussion of portfolio composition will focus on fixed maturities.

Selected information concerning the fixed maturity portfolio is as follows:

Fixed Maturities
Fixed Maturity Portfolio Selected Information

	At December 31,	
	2017	2016
Average annual effective yield ⁽¹⁾	5.60%	5.74%
Average life, in years, to:		
Next call ⁽²⁾	17.5	17.6
Maturity ⁽²⁾	19.1	19.8
Effective duration to:		
Next call ^(2, 3)	10.8	10.4
Maturity ^(2, 3)	11.5	11.3

(1) Tax-equivalent basis, where the yield on tax-exempt securities is adjusted to produce a yield equivalent to the pretax yield on taxable securities.

(2) Torchmark calculates the average life and duration of the fixed maturity portfolio two ways:

(a) based on the next call date which is the next call date for callable bonds and the maturity date for noncallable bonds, and

(b) based on the maturity date of all bonds, whether callable or not.

(3) Effective duration is a measure of the price sensitivity of a fixed-income security to a particular change in interest rates.

Credit Risk Sensitivity. The following tables summarize certain information about the major corporate sectors and security types held in our fixed maturity portfolio at December 31, 2017 and 2016.

Fixed Maturities by Sector
At December 31, 2017
(Dollar amounts in thousands)

	Below Investment Grade				Total Fixed Maturities				% of Total Fixed Maturities	
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	At Amortized Cost	At Fair Value
Corporates:										
Financial										
Insurance - life, health, P&C	\$ 66,489	\$ 3,896	\$ (3,650)	\$ 66,735	\$ 2,018,315	\$ 346,364	\$ (4,588)	\$ 2,360,091	14	14
Banks	27,104	—	(2,727)	24,377	747,249	117,724	(3,007)	861,966	5	5
Other financial	74,956	—	(17,661)	57,295	853,583	74,765	(18,524)	909,824	6	6
Total financial.....	168,549	3,896	(24,038)	148,407	3,619,147	538,853	(26,119)	4,131,881	25	25
Utilities										
Electric.....	20,713	1,159	—	21,872	1,463,872	306,812	(1,275)	1,769,409	10	11
Gas and water	—	—	—	—	520,418	64,726	(120)	585,024	3	3
Total utilities.....	20,713	1,159	—	21,872	1,984,290	371,538	(1,395)	2,354,433	13	14
Industrial - Energy										
Pipelines.....	40,590	937	(1,092)	40,435	880,379	117,765	(2,320)	995,824	6	6
Exploration and production.....	28,174	1,180	(85)	29,269	527,581	79,784	(2,620)	604,745	4	4
Oil field services	33,867	—	(6,004)	27,863	83,722	11,074	(6,004)	88,792	1	1
Refiner.....	—	—	—	—	73,106	17,430	—	90,536	—	—
Driller	54,561	87	(14,448)	40,200	54,561	87	(14,448)	40,200	—	—
Total energy.....	157,192	2,204	(21,629)	137,767	1,619,349	226,140	(25,392)	1,820,097	11	11
Industrial - Basic materials										
Chemicals.....	—	—	—	—	541,785	59,216	(20)	600,981	3	3
Metals and mining	57,438	7,727	—	65,165	387,134	85,105	—	472,239	3	3
Forestry products and paper	—	—	—	—	112,175	16,911	—	129,086	1	1
Total basic materials.	57,438	7,727	—	65,165	1,041,094	161,232	(20)	1,202,306	7	7
Industrial - Consumer, non-cyclical.....	21,334	—	(4,498)	16,836	1,834,778	192,887	(6,494)	2,021,171	12	12
Other industrials	47,136	2,965	—	50,101	1,326,051	179,694	(671)	1,505,074	9	9
Industrial - Transportation	26,443	1,581	(162)	27,862	553,435	90,211	(195)	643,451	3	4
Other corporate sectors..	143,995	5,076	(9,387)	139,684	1,310,445	123,588	(13,236)	1,420,797	9	8
Total corporates.....	642,800	24,608	(59,714)	607,694	13,288,589	1,884,143	(73,522)	15,099,210	89	90
Other fixed maturities:										
Government (U.S., municipal, and foreign) ...	306	—	(105)	201	1,501,865	147,772	(1,507)	1,648,130	10	9
Collateralized debt obligations	59,150	20,084	(7,653)	71,581	59,150	20,084	(7,653)	71,581	—	—
Other asset-backed securities	—	—	—	—	144,040	4,790	—	148,830	1	1
Mortgage-backed securities ⁽¹⁾	—	—	—	—	1,457	118	(1)	1,574	—	—
Total fixed maturities.	\$ 702,256	\$ 44,692	\$ (67,472)	\$ 679,476	\$14,995,101	\$2,056,907	\$ (82,683)	\$16,969,325	100	100

(1) Includes GNMA's

Fixed Maturities by Sector
At December 31, 2016
(Dollar amounts in thousands)

	Below Investment Grade				Total Fixed Maturities				% of Total Fixed Maturities	
	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	At Amortized Cost	At Fair Value
Corporates:										
Financial										
Insurance - life, health, P&C	\$ 58,400	\$ 1,760	\$ (4,003)	\$ 56,157	\$ 2,030,188	\$ 217,377	\$ (16,783)	\$ 2,230,782	15	15
Banks	41,558	512	(7,218)	34,852	681,422	71,828	(11,692)	741,558	5	5
Other financial	74,955	—	(18,589)	56,366	623,836	39,215	(24,628)	638,423	4	4
Total financial.....	174,913	2,272	(29,810)	147,375	3,335,446	328,420	(53,103)	3,610,763	24	24
Utilities										
Electric.....	21,300	486	—	21,786	1,433,742	219,154	(9,384)	1,643,512	10	11
Gas and water	—	—	—	—	470,804	31,345	(3,464)	498,685	3	3
Total utilities.....	21,300	486	—	21,786	1,904,546	250,499	(12,848)	2,142,197	13	14
Industrial - Energy										
Pipelines.....	45,394	87	(3,297)	42,184	809,300	67,313	(11,431)	865,182	6	6
Exploration and production.....	28,954	182	(744)	28,392	531,754	43,009	(11,806)	562,957	4	4
Oil field services	33,880	—	(6,483)	27,397	83,753	7,624	(6,483)	84,894	1	1
Refiner.....	—	—	—	—	62,977	9,721	(7)	72,691	—	—
Driller	54,642	322	(14,597)	40,367	54,642	322	(14,597)	40,367	—	—
Total energy	162,870	591	(25,121)	138,340	1,542,426	127,989	(44,324)	1,626,091	11	11
Industrial - Basic materials										
Chemicals.....	—	—	—	—	481,127	21,538	(10,204)	492,461	3	3
Metals and mining	107,102	491	(2,195)	105,398	389,908	25,247	(2,613)	412,542	3	3
Forestry products and paper	—	—	—	—	112,702	10,270	(415)	122,557	1	1
Total basic materials.....	107,102	491	(2,195)	105,398	983,737	57,055	(13,232)	1,027,560	7	7
Industrial - Consumer, non-cyclical.....	—	—	—	—	1,629,706	101,254	(31,938)	1,699,022	11	11
Other industrials	80,311	4,066	(1,327)	83,050	1,282,000	115,119	(14,412)	1,382,707	9	9
Industrial - Transportation	26,675	—	(2,918)	23,757	494,527	59,067	(4,709)	548,885	4	4
Other corporate sectors..	116,696	1,076	(6,063)	111,709	1,211,166	91,526	(20,256)	1,282,436	9	8
Total corporates.....	689,867	8,982	(67,434)	631,415	12,383,554	1,130,929	(194,822)	13,319,661	88	88
Other fixed maturities:										
Government (U.S., municipal, and foreign) ...	551	—	(194)	357	1,686,021	129,064	(10,539)	1,804,546	12	12
Collateralized debt obligations	60,726	13,062	(10,285)	63,503	60,726	13,062	(10,285)	63,503	—	—
Other asset-backed securities	—	—	—	—	53,786	530	(337)	53,979	—	—
Mortgage-backed securities ⁽¹⁾	—	—	—	—	3,963	210	(1)	4,172	—	—
Total fixed maturities.	\$ 751,144	\$ 22,044	\$ (77,913)	\$ 695,275	\$14,188,050	\$1,273,795	\$ (215,984)	\$ 15,245,861	100	100

(1) Includes GNMA's

At December 31, 2017, fixed maturities had a fair value of \$17.0 billion, compared with \$15.2 billion at December 31, 2016. The net unrealized gain position in the fixed maturity portfolio increased from \$1.1 billion at December 31, 2016 to \$2.0 billion at December 31, 2017, primarily as a result of a decrease in credit spreads. The December 31, 2017 net unrealized gain consisted of gross unrealized gains of \$2.1 billion offset by \$83 million of gross unrealized losses, compared with the December 31, 2016 net unrealized gain which consisted of a gross unrealized gain of \$1.3 billion and a gross unrealized loss of \$216 million.

Corporate securities, which consist of bonds and redeemable preferred stocks, were the largest component of the fixed maturity portfolio, representing 89% of amortized cost and 90% of fair value. The remainder of the portfolio is

invested primarily in securities issued by the U.S. government and U.S. municipalities. The Company holds insignificant amounts in foreign government bonds, collateralized debt obligations, asset-backed securities, and agency mortgage-backed securities. Corporate securities are diversified over a variety of industry sectors and issuers. As shown in the chart above, financial, utility, and energy sectors represented approximately 50% of the portfolio. At December 31, 2017, the total fixed maturity portfolio consists of 596 issuers, with 220 issuers within the financial, utility, and energy sectors.

The net unrealized gain of the fixed maturity portfolio increased \$916 million from December 31, 2016. The financial, utility, energy, and basic materials sectors experienced increases of \$237 million, \$132 million, \$117 million, and \$117 million respectively, in net unrealized gains from December 31, 2016 to December 31, 2017. The fair value of the entire portfolio increased 11% for the period. Over the past year, oil and many other commodity prices have increased meaningfully to the benefit of our holdings in the energy and basic materials sectors. While a sustained period of low prices might lead to some downgrades in ratings, we do not currently anticipate any losses from defaults or write-downs in the foreseeable future.

For more information about our fixed maturity portfolio by component at December 31, 2017 and 2016, including a discussion of other-than-temporary impairments, an analysis of unrealized investment losses and a schedule of maturities, see *Note 4—Investments*.

An analysis of the fixed maturity portfolio by a composite rating at December 31, 2017 is shown in the following table. The composite rating for each security, other than private-placement securities managed by third parties, is the average of the security's ratings as assigned by Moody's Investor Service, Standard & Poor's, Fitch Ratings, and Dominion Bond Rating Service, LTD. The ratings assigned by these four nationally recognized statistical rating organizations are evenly weighted when calculating the average. The composite quality rating is created using a methodology developed by Torchmark Corporation using ratings from the various rating agencies noted above. The composite quality rating is not a Standard & Poor's credit rating. Standard & Poor's does not sponsor, endorse or promote the composite quality rating and shall not be liable for any use of the composite quality rating. Included in the chart below are private placement fixed maturity holdings of \$591 million at amortized cost (\$613 million at fair value) for which the ratings were assigned by the third party managers.

Fixed Maturities by Rating
At December 31, 2017
(Dollar amounts in thousands)

	<u>Amortized Cost</u>	<u>%</u>	<u>Fair Value</u>	<u>%</u>
Investment grade:				
AAA	\$ 649,559	4	\$ 689,356	4
AA	1,095,502	7	1,222,148	7
A	4,139,252	28	4,959,570	29
BBB+	3,493,309	23	3,936,939	23
BBB	3,302,118	22	3,696,880	22
BBB-	1,613,105	11	1,784,956	11
Investment grade	<u>14,292,845</u>	<u>95</u>	<u>16,289,849</u>	<u>96</u>
Below investment grade:				
BB	413,425	3	397,063	2
B	152,454	1	133,582	1
Below B	136,377	1	148,831	1
Below investment grade	<u>702,256</u>	<u>5</u>	<u>679,476</u>	<u>4</u>
	<u><u>\$ 14,995,101</u></u>	<u><u>100</u></u>	<u><u>\$ 16,969,325</u></u>	<u><u>100</u></u>

Of the \$15.0 billion of fixed maturities at amortized cost as of December 31, 2017, \$14.3 billion or 95% were investment grade with an average rating of A-. Below-investment-grade bonds were \$702 million with an average rating of B+. Below-investment-grade bonds at amortized cost were 15% of our shareholders' equity, excluding the effect of unrealized gains and losses on fixed maturities as of December 31, 2017. Overall, the total portfolio had a weighted average quality rating of BBB+ based on amortized cost, the same as at the end of 2016.

An analysis of changes in our portfolio of below-investment grade fixed maturities at amortized cost is as follows:

Below-Investment Grade Fixed Maturities
(Dollar amounts in thousands)

	Year Ended December 31,	
	2017	2016
Balance at beginning of year	\$ 751,144	\$ 640,150
Downgrades by rating agencies	61,691	179,077
Upgrades by rating agencies	(55,345)	(58,626)
Disposals	(59,420)	(13,860)
Write down of other-than-temporarily impaired securities	(245)	—
Amortization	4,431	4,403
Balance at end of year	<u>\$ 702,256</u>	<u>\$ 751,144</u>

Our investment policy regarding fixed maturities is to acquire only investment-grade obligations. Thus, any increases in below investment-grade issues are a result of ratings downgrades of existing holdings. We are not a party to any credit default swaps or other derivative contracts. We do not participate in securities lending, we have no off-balance sheet investments, and we do not have any exposure to European sovereign debt at December 31, 2017. Our exposure to Puerto Rican obligations is insignificant.

Market Risk Sensitivity. Torchmark's investment securities are exposed to interest rate risk, meaning the effect of changes in financial market interest rates on the current fair value of the company's investment portfolio. Since 95% of the book value of our investments is attributable to fixed maturity investments (and virtually all of these investments are fixed-rate investments), the portfolio is highly subject to market risk. Declines in market interest rates generally result in the fair value of the investment portfolio rising and increases in interest rates cause the fair value to decline. Under normal market conditions, we do not expect to realize these unrealized gains and losses because we have the ability and the intent to hold these investments to maturity. The long-term nature of our insurance policy liabilities and strong cash-flow operating position substantially mitigate any future need to liquidate portions of the portfolio. The increase or decrease in the fair value of insurance liabilities and debt due to increases or decreases in market interest rates largely offsets the impact of rates on the investment portfolio. However, as is permitted by GAAP, these liabilities are not recorded at fair value.

The following table illustrates the market risk sensitivity of our interest-rate sensitive fixed maturity portfolio at December 31, 2017 and 2016. This table measures the effect of a parallel shift in interest rates (as represented by the U.S. Treasury curve) on the fair value of the fixed maturity portfolio. The data measures the change in fair value arising from an immediate and sustained change in interest rates in increments of 100 basis points.

Market Value of Fixed Maturity Portfolio
(Dollar amounts in thousands)

Change in Interest Rates ⁽¹⁾	At December 31,	
	2017	2016
(200)	\$ 21,455,515	\$ 19,126,303
(100)	19,024,031	17,030,458
0	16,969,325	15,245,861
100	15,221,207	13,716,023
200	13,723,745	12,395,635

(1) In basis points.

FINANCIAL CONDITION

Liquidity. Liquidity provides Torchmark with the ability to meet on demand the cash commitments required by its business operations and financial obligations. Our liquidity is primarily derived from three sources: positive cash flow from operations, a portfolio of marketable securities, and a line of credit facility.

Insurance Subsidiary Liquidity. The operations of our insurance subsidiaries have historically generated substantial cash inflows in excess of immediate cash needs. Sources of cash flows for the insurance subsidiaries include primarily premium and investment income. Cash outflows from operations include policy benefit payments, commissions, administrative expenses, and taxes. The funds to provide for policy benefits, the majority of which are paid in future periods, are invested primarily in long-term fixed maturities to meet these long-term obligations. In addition to investment income, maturities and scheduled repayments in the investment portfolio are sources of cash. Excess cash available from the insurance subsidiaries' operations is generally distributed as a dividend to the Parent Company, subject to regulatory restriction. The dividends are generally paid in amounts equal to the subsidiaries' prior year statutory net income excluding realized capital gains. While the leading source of the excess cash is investment income, due to our high underwriting margins and effective expense control, a significant portion of the excess cash also comes from underwriting income.

Parent Company Liquidity. Cash flows from the insurance subsidiaries are used to pay interest and principal repayments on Parent Company debt, operating expenses of the Parent, and Parent Company dividends to Torchmark shareholders. In 2017, the Parent received \$454 million of cash dividends from its subsidiaries, compared with \$438 million in 2016 and \$466 million in 2015. Including transfers from other subsidiaries and after paying debt obligations, shareholder dividends, and other expenses (but before share repurchases), the Parent Company had excess cash flow in 2017 of approximately \$330 million, compared with \$311 million in 2016 and \$358 million in 2015.

Parent Company cash flow in excess of its operating requirements is available for other corporate purposes, such as insurance subsidiary capital or financing needs, strategic acquisitions, additional shareholder dividends, or share repurchases. In 2018, it is expected that the Parent Company will receive approximately \$450 million in dividends and transfers from subsidiaries and that approximately \$320 to \$330 million will be available as excess cash flow. Certain restrictions exist on the payment of these dividends. For more information on the restrictions on the payment of dividends by subsidiaries, see the *Restrictions* section of *Note 12—Shareholders' Equity*. Although these restrictions exist, dividend availability from subsidiaries historically has been more than sufficient for the cash flow needs of the Parent Company.

Short-Term Borrowings. An additional source of parent company liquidity is a line of credit facility with a group of lenders which allows unsecured borrowings and stand-by letters of credit up to \$750 million, which could be extended up to \$1 billion. While Torchmark can request the extension, it is not guaranteed. In May 2016, Torchmark amended the facility to extend the maturity date to May 2021. The amendment also allowed for an additional \$100 million term loan as discussed under the caption *Credit Facility* in *Note 11—Debt*. The facility is further designated as a back-up line of credit for a commercial paper program as well as the stand-by letters of credit as discussed below. As of December 31, 2017, we had available \$249 million of additional borrowing capacity under this facility, compared with \$310 million a year earlier. There have been no difficulties in accessing the commercial paper market during the three years ended December 31, 2017.

In summary, Torchmark expects to have readily available funds for 2018 and the foreseeable future to conduct its operations and to maintain target capital ratios in the insurance subsidiaries through internally generated cash flow and the credit facility. In the unlikely event that more liquidity is needed, the Company could generate additional funds through multiple sources including, but not limited to, the issuance of additional debt, additional borrowings on our short-term credit facility, and intercompany borrowing.

Consolidated Liquidity. Consolidated net cash inflows provided from continuing operations were \$1.4 billion in 2017, compared with \$1.2 billion in 2016 and \$1.1 billion in 2015. In addition to cash inflows from operations, our companies received proceeds from maturities, calls, and repayments of fixed maturities in the amount of \$489 million in 2017, compared with \$236 million in 2016 and \$376 million in 2015.

Our cash and short-term investments were \$246 million at year-end 2017 and \$148 million at year-end 2016. Additionally, we have a portfolio of marketable fixed securities that are available for sale in the event of an unexpected need. These securities had a fair value of \$17.0 billion at December 31, 2017. However, our strong cash flows from operations, investment maturities, and the availability of our credit line make any need to sell securities for liquidity unlikely.

Off-Balance Sheet Arrangements. As a part of its aforementioned credit facility, Torchmark had outstanding \$177 million in stand-by letters of credit at December 31, 2017 and 2016. These letters are issued among our subsidiaries, one of which is an offshore captive reinsurer, and have no impact on company obligations as a whole. Any future regulatory changes that restrict the use of off-shore captive reinsurers might require Torchmark to obtain third-party financing, which could cause an insignificant increase in financing costs.

As of December 31, 2017, we had no unconsolidated affiliates and no guarantees of the obligations of third party entities. All of our guarantees were guarantees of the performance of consolidated subsidiaries, as disclosed in *Note 15—Commitments and Contingencies*.

The following table presents information about future payments under our contractual obligations for the selected periods as of December 31, 2017.

Contractual Obligations
(Dollar amounts in thousands)

	<u>Actual Liability</u>	<u>Total Payments</u>	<u>Less than One Year</u>	<u>One to Three Years</u>	<u>Three to Five Years</u>	<u>More than Five Years</u>
Fixed and determinable:						
Debt—principal ⁽¹⁾	\$ 1,460,268	\$ 1,475,634	\$ 328,625	\$ 308,897	\$ 227,500	\$ 610,612
Debt—interest ⁽²⁾	6,837	1,134,369	73,967	111,475	87,988	860,939
Capital leases	—	—	—	—	—	—
Operating leases	—	16,564	3,483	6,422	4,829	1,830
Purchase obligations ⁽³⁾ ...	33,846	290,999	27,326	12,455	4,382	246,836
Postretirement obligations ⁽⁴⁾	250,595	292,824	21,603	48,572	55,059	167,590
Future insurance obligations ⁽⁵⁾	13,439,472	52,462,823	1,584,774	3,074,789	2,955,996	44,847,264
Total	<u>\$15,191,018</u>	<u>\$ 55,673,213</u>	<u>\$ 2,039,778</u>	<u>\$ 3,562,610</u>	<u>\$ 3,335,754</u>	<u>\$46,735,071</u>

(1) Debt is itemized in *Note 11—Debt*.

(2) Interest on debt is based on our fixed contractual obligations.

(3) Purchase obligations include various long-term non-cancelable purchase commitments as well as commitments to provide capital for low-income housing tax credit interests.

(4) Pension obligations are primarily liabilities in trust funds that are calculated in accordance with the terms of the pension plans. They are offset by invested assets in the trusts, which are funded through periodic contributions by Torchmark in a manner which will provide for the settlement of the obligations as they become due. Therefore, our obligations are offset by those assets when reported on Torchmark's *Consolidated Balance Sheets*. At December 31, 2017, these pension obligations were \$603 million, but there were also assets of \$378 million in the pension entities. The schedule of pension benefit payments covers ten years and is based on the same assumptions used to measure the pension obligations, except there is no interest assumption because the payments are undiscounted. There are also obligations for benefits other than pensions with a liability of \$26 million. Please refer to *Note 9—Postretirement Benefits* for more information on pension obligations.

(5) Future insurance obligations consist primarily of estimated future contingent benefit payments on policies in force at December 31, 2017. These estimated payments were computed using assumptions for future mortality, morbidity and persistency. The actual amount and timing of such payments may differ significantly from the estimated amounts shown. Management believes that the assets supporting the liability of \$13.4 billion at December 31, 2017, along with future premiums and investment income, will be sufficient to fund all future insurance obligations.

Capital Resources. Torchmark's capital structure consists of short-term debt (the commercial paper facility described in *Note 11—Debt* and the current maturity of funded debt), long-term funded debt, and shareholders' equity. A complete analysis and description of long-term debt issues outstanding is presented in *Note 11—Debt*.

Debt: The carrying value of the long-term debt was \$1.1 billion at December 31, 2017, the same as a year earlier.

On November 17, 2017, Torchmark completed the issuance and sale of \$125 million in aggregate principal of Torchmark's 5.275% Junior Subordinated Debentures due 2057. The debentures were sold in a private placement pursuant to exemptions from the registration requirements of the Securities Act of 1933. The initial purchaser of the debentures was outside the United States. The net proceeds from the sale of the debentures were \$123.3 million, after giving effect to the discount payable to the initial purchaser and expenses of the offering of the debentures. Torchmark used the net proceeds from the offering of the debentures to repay the \$125 million outstanding principal of the 5.875% Junior Subordinated Debentures that were due December 15, 2052 and that were callable beginning December 15, 2017.

On April 5, 2016, Torchmark completed the issuance and sale of \$300 million aggregate principal amount of Torchmark's 6.125% Junior Subordinated Debentures due 2056. The debentures were sold pursuant to Torchmark's shelf registration statement on Form S-3, filed September 25, 2015. The net proceeds from the sale of the debentures were \$290 million, after giving effect to the underwriting discount and estimated expenses of the offering of the debentures. Torchmark used the net proceeds from the offering of the debentures to repay the \$250 million outstanding principal amount plus accrued interest of \$8 million on its 6.375% Senior Notes that were due June 15, 2016. The remaining proceeds were used for general corporate purposes.

Subsidiary Capital: For the past several years, our insurance subsidiaries have targeted a capital ratio of approximately 325% of Company Action Level regulatory capital under Risk-Based Capital (RBC) standards, a formula designed by insurance regulatory authorities to monitor the adequacy of capital. At December 31, 2017, our insurance subsidiaries had an aggregate RBC ratio of 314%, a decrease in the ratio from the prior year of 324% due to the reduction in deferred tax assets as a result of the Tax Legislation previously discussed in the *Results of Operations* in this report. Should the NAIC adjust the RBC factors in 2018, as expected, to take into account the lower tax rate, we would expect a further reduction in our consolidated RBC ratio for the year ending December 31, 2018. At this time, target RBC levels for 2018 are yet to be determined pending discussion with regulators and rating agencies. Management believes more than sufficient liquidity exists at the Parent Company to make additional contributions as necessary to maintain the targeted ratio.

Shareholder's Equity: As noted under the caption *Analysis of Share Repurchases* in this report, we have an ongoing share repurchase program. Under this program, we acquired 4 million shares at a cost of \$325 million in 2017, 5 million shares at a cost of \$311 million in 2016, and 6 million shares for \$359 million in 2015. The majority of purchased shares are retired each year. Please refer to the description of our share repurchase program under the caption *Summary of Operations* in this report.

Torchmark has continually increased the quarterly dividend on its common shares over the past three years. In the first quarter of 2015, it was increased to \$0.135 per share from \$0.1267 per share. In the first quarter of 2016, it was raised to \$0.14 per share. Finally, in the first quarter of 2017, dividends were raised to \$0.15 per share.

Shareholders' equity was \$6.2 billion at December 31, 2017, compared with \$4.6 billion at December 31, 2016, a \$1.7 billion or 36% increase. During the twelve months since December 31, 2016, shareholders' equity was reduced by \$325 million in share purchases under the repurchase program and \$88 million to offset the dilution from stock option exercises. However, it was increased by \$1.5 billion of net income, \$874 million of which was attributed to a tax adjustment as a result of the Tax Legislation and \$870 million of after-tax unrealized gains, of which \$275 million was attributed to a tax adjustment as a result of the Tax Legislation.

We plan to use excess cash available at the Parent Company as efficiently as possible in the future. Possible uses of excess cash flow include, but are not limited to, share repurchases, acquisitions, increases in shareholder dividends, investment in securities, or repayment of short-term debt. We will determine the best use of excess cash after ensuring that targeted capital levels are maintained in our companies. If market conditions are favorable, we currently expect that share repurchases will continue to be a primary use of those funds.

We maintain a significant available-for-sale fixed maturity portfolio to support our insurance policyholders' liabilities. Current accounting guidance requires that we revalue our portfolio to fair market value at the end of each accounting period. The period-to-period changes in fair value, net of their associated impact on deferred acquisition costs and income tax, are reflected directly in shareholders' equity. Changes in the fair value of the portfolio can result from changes in interest rates and liquidity in financial markets. While invested assets are revalued, accounting rules do not permit interest-bearing insurance policy liabilities to be valued at fair value in a consistent manner as that of assets, with changes in value applied directly to shareholders' equity.

Due to the size of our policy liabilities in relation to our shareholders' equity, this inconsistency in measurement usually has a material impact on the reported value of shareholders' equity. If these liabilities were revalued in the same manner as the assets, the effect on equity would be largely offset. Fluctuations in interest rates cause undue volatility in the period-to-period presentation of our shareholders' equity, capital structure, and financial ratios which would be essentially removed if interest-bearing liabilities were valued in the same manner as assets. From time to time, the market value of our fixed maturity portfolio may be depressed as a result of bond market illiquidity which could result in a significant decrease in shareholders' equity. Because of the long-term nature of our fixed maturities and liabilities and the strong cash flows consistently generated by our insurance subsidiaries, we have the intent and ability to hold our securities to maturity. As such, we do not expect to incur losses due to fluctuations in market value of fixed maturities caused by interest rate changes and temporarily illiquid markets. Accordingly, our management, credit rating agencies, lenders, many industry analysts, and certain other financial statement users prefer to remove the effect of this accounting rule when analyzing our balance sheet, capital structure, and financial ratios.

The following table presents selected data related to our capital resources. Additionally, the table presents the effect of this accounting guidance on relevant line items, so that investors and other financial statement users may determine its impact on Torchmark's capital structure. Excluding the effect of unrealized gains and losses on the fixed maturity portfolio from shareholders' equity is considered non-GAAP. Below we include the reconciliation to GAAP.

Selected Financial Data

(Dollar amounts in thousands except per share and percentage data)

	At December 31, 2017		At December 31, 2016		At December 31, 2015	
	GAAP	Effect of Accounting Rule Requiring Revaluation ⁽¹⁾	GAAP	Effect of Accounting Rule Requiring Revaluation ⁽¹⁾	GAAP	Effect of Accounting Rule Requiring Revaluation ⁽¹⁾
Fixed maturities	\$16,969,325	\$ 1,974,224	\$15,245,861	\$ 1,057,811	\$13,758,024	\$ 506,153
Deferred acquisition costs ⁽²⁾	3,958,063	(10,819)	3,783,158	(10,281)	3,617,135	(7,869)
Total assets	23,474,985	1,963,405	21,436,087	1,047,530	19,853,213	498,284
Short-term debt	328,067	—	264,475	—	490,129	—
Long-term debt	1,132,201	—	1,133,165	—	743,733	—
Shareholders' equity	6,231,421	1,551,090	4,566,861	680,894	4,055,552	323,885
Book value per diluted share.....	52.95	13.18	37.76	5.63	32.71	2.62
Debt to capitalization ⁽³⁾	19.0%	(4.8)%	23.4%	(3.1)%	23.3%	(1.5)%
Diluted shares outstanding.....	117,696		120,958		123,996	
Actual shares outstanding.....	114,593		118,031		122,370	

(1) Amount added to (deducted from) comprehensive income to produce the stated GAAP item.

(2) Includes the value of insurance purchased.

(3) Torchmark's debt covenants require that the effect of the accounting guidance requiring revaluation be removed to determine this ratio. This ratio is computed by dividing total debt by the sum of debt and shareholders' equity.

Torchmark's ratio of earnings before interest and taxes to interest requirements (times interest earned) was 10.8 times in 2017, compared with 10.3 times in 2016 and 11.0 times in 2015 based on continuing operations. This times-interest-earned ratio is computed by dividing interest expense into the sum of pre-tax income from continuing operations and interest expense. A discussion of our interest expense is included in the discussion of financing costs under the caption *Investments* in this report.

Financial Strength Ratings. The financial strength of our major insurance subsidiaries is rated by Standard & Poor's and A. M. Best. The following chart presents these ratings for our five largest insurance subsidiaries at December 31, 2017.

	Standard & Poor's	A.M Best
Liberty	AA-	A+ (Superior)
Globe	AA-	A+ (Superior)
United American	AA-	A+ (Superior)
American Income	AA-	A+ (Superior)
Family Heritage	NR	A+ (Superior)

A.M. Best states that it assigns an A+ (Superior) rating to insurance companies that have, in its opinion, a superior ability to meet their ongoing insurance obligations.

The AA financial strength rating category is assigned by Standard & Poor's Corporation (S&P) to those insurers which have very strong capacity to meet its financial commitments which differs from the highest-rated insurers only to a small degree. An insurer rated A has strong capacity to meet its financial commitments but it is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than insurers in higher-rated categories. The plus sign (+) or minus sign (-) shows the relative standing within the major rating category.

During the fourth quarter of 2017, S&P reviewed our operations and financial outlook. Based on their review, they confirmed our "AA-" financial strength ratings at our insurance subsidiaries and Torchmark Corporation's senior debt "A" credit rating.

OTHER ITEMS

Litigation. Torchmark and its subsidiaries are subject to being named as parties to pending or threatened litigation, much of which involves punitive damage claims based upon allegations of agent misconduct at the insurance subsidiaries. Such punitive damage claims may have the potential for significant adverse results since Torchmark and its subsidiaries operate in jurisdictions where large punitive damage awards bearing little or no relation to actual damages continue to be awarded. This bespeaks caution since it is impossible to predict the likelihood or extent of punitive damages that may be awarded if liability is found in any given case. Based upon information presently available, and in light of legal and other factual defenses available to Torchmark and its subsidiaries, contingent liabilities arising from threatened and pending litigation are not presently considered by us to be material. For more information concerning litigation, please refer to *Note 15—Commitments and Contingencies* .

CRITICAL ACCOUNTING POLICIES

Future Policy Benefits: Due to the long-term nature of insurance contracts, our insurance companies are liable for policy benefit payments that will be made in the future. The liability for future policy benefits is determined by standard actuarial procedures common to the life insurance industry. The accounting policies for determining this liability are disclosed in *Note 1—Significant Accounting Policies*.

Approximately 87% of our liabilities for future policy benefits at December 31, 2017 were traditional insurance liabilities where the liability is determined as the present value of future benefits less the present value of the portion of the gross premium required to pay for such benefits. The assumptions used in estimating the future benefits for this portion of business are set at the time of contract issue. These assumptions are “locked in” and are not revised for the lifetime of the contracts, except where there is a premium deficiency, as defined in *Note 1—Significant Accounting Policies* under the caption *Future Policy Benefits*. Otherwise, variability in the accrual of policy reserve liabilities after policy issuance is caused only by variability of the inventory of in force policies. Torchmark did not have a premium deficiency event for its traditional business during the three years ended December 31, 2017.

The remaining portion of liabilities for future policy benefits pertains to business accounted for as deposit business, where the recorded liability is the fund balance attributable to the benefit of policyholders as determined by the policy contract at the financial statement date. Accordingly, there are no assumptions used to determine the future policy benefit liability for deposit business.

Deferred Acquisition Costs: Certain costs of acquiring new business are deferred and recorded as an asset. Deferred acquisition costs consist primarily of sales commissions and other underwriting costs related to the successful issuance of a new insurance contract as indicated in *Note 1—Significant Accounting Policies* under the caption *Deferred Acquisition Costs* in the *Notes to Consolidated Financial Statements*. Additionally, the cost of acquiring blocks of insurance business or insurance business through the purchase of other companies, known as the value of insurance purchased, is included in deferred acquisition costs. Our policies for accounting for deferred acquisition costs and the associated amortization are reported under the same caption in *Note 1—Significant Accounting Policies*.

Over 99% of our recorded amounts for deferred acquisition costs at December 31, 2017 were related to traditional products and are being amortized over the premium-paying period in proportion to the present value of actual historic and estimated future gross premiums. The projection assumptions for this business are set at the time of contract issue. These assumptions are “locked-in” at that time and, except where there is a loss recognition issue, are not revised for the lifetime of the contracts. Absent a premium deficiency, variability in amortization after policy issuance is caused only by variability in premium volume. We have not recorded a deferred acquisition cost loss recognition event for assets related to this business for any period in the three years ended December 31, 2017.

Less than 1% of deferred acquisition costs pertain to deposit business for which deferred acquisition costs are amortized over the estimated lives of the contracts in proportion to actual and estimated future gross profits. These contracts are not subject to lock-in. The assumptions must be updated when actual experience or other evidence suggests that earlier estimates should be revised. Revisions related to our deposit business assets have not had a material impact on the amortization of deferred acquisition costs during the three years ended December 31, 2017.

Policy Claims and Other Benefits Payable: This liability consists of known benefits currently payable and an estimate of claims that have been incurred but not yet reported to us. The estimate of unreported claims is based on prior experience and is made after careful evaluation of all information available to us. However, the factors upon which these estimates are based can be subject to change from historical patterns. Factors involved include the litigation environment, regulatory mandates, and the introduction of policy types for which claim patterns are not well established, and medical trend rates and medical cost inflation as they affect our health claims. Changes in these estimates, if any, are reflected in the earnings of the period in which the adjustment is made. We believe that the estimates used to produce the liability for claims and other benefits, including the estimate of unsubmitted claims, are the most appropriate under the circumstances. However, there is no certainty that the resulting stated liability will be our ultimate obligation. At this time, we do not expect any change in this estimate to have a material impact on earnings or financial position consistent with our historical experience.

Valuation of Fixed Maturities: We hold a substantial investment in high-quality fixed maturities to provide for the funding of our future policy contractual obligations over long periods of time. While these securities are generally expected to be held to maturity, they are classified as available for sale and are sold from time to time, primarily to manage risk. We report this portfolio at fair value. Fair value is the price that we would expect to receive upon sale of the asset in an orderly transaction. The fair value of the fixed maturity portfolio is primarily affected by changes in interest rates in financial markets, having a greater impact on longer-term maturities. Because of the size of our fixed maturity portfolio, small changes in rates can have a significant effect on the portfolio and the reported financial position of the Company. This impact is disclosed in 100 basis point increments under the caption *Market Risk Sensitivity* in this report. However, as discussed under the caption *Financial Condition* in this report, we believe these unrealized fluctuations in value have no meaningful impact on our actual financial condition and, as such, we remove them from consideration when viewing our financial position and financial ratios.

At times, the values of our fixed maturities can also be affected by illiquidity in the financial markets. Illiquidity would contribute to a spread widening, and accordingly unrealized losses, on many securities that we would expect to be fully recoverable. Even though our fixed maturity portfolio is available for sale, we have the ability and intent to hold the securities until maturity as a result of our strong and stable cash flows generated from our insurance products. Considerable information concerning the policies, procedures, classification levels, and other relevant data concerning the valuation of our fixed maturity investments is presented in *Note 1—Significant Accounting Policies* and in *Note 4—Investments* under the captions *Fair Value Measurements* in both notes.

Impairment of Investments: We continually monitor our investment portfolio for investments where fair value has declined below carrying value and that have become impaired in value. While the values of the investments in our portfolio constantly fluctuate due to market conditions, an other-than-temporary impairment charge is recorded only when a security has experienced a decline in fair market value which is deemed to be other than temporary. The policies and procedures that we use to evaluate and account for impairments of investments are disclosed in *Note 1—Significant Accounting Policies* and the discussions under the captions *Investments* and *Realized Gains and Losses* in this report. While every effort is made to make the best estimate of status and value with the information available regarding an other-than-temporary impairment, it is difficult to predict the future prospects of a distressed or impaired security.

Defined benefit pension plans: We maintain funded defined benefit plans covering most full-time employees. We also have unfunded nonqualified defined benefit plans covering certain key and other employees. Our obligations under these plans are determined actuarially based on specified actuarial assumptions. In accordance with GAAP, an expense is recorded each year as these pension obligations grow due to the increase in the service period of employees and the interest cost associated with the passage of time. These obligations are offset, at least in part, by the growth in value of the assets in the funded plans. At December 31, 2017, our gross liability under these plans was \$603 million, but was offset by assets of \$378 million.

The actuarial assumptions used in determining our obligations for pensions include employee mortality and turnover, retirement age, the expected return on plan assets, projected salary increases, and the discount rate at which future obligations could be settled. These assumptions have an important effect on the pension obligation. A decrease in the discount rate or rate of return on plan assets will cause an increase in the pension obligation. A decrease in projected salary increases will cause a decrease in this obligation. Small changes in assumptions may cause significant differences in reported results for these plans. For example, a sensitivity analysis is presented below for the impact of change in the discount rate and the long-term rate of return on assets assumed on our defined benefit pension plans expense for the year 2017 and projected benefit obligation as of December 31, 2017.

Pension Assumptions
(Dollar amounts in thousands)

Assumption	% Change	Impact on Expense	Impact on Projected Benefit Obligation
Discount Rate ⁽¹⁾ :			
Increase	0.25	\$ (2,890)	\$ (23,697)
Decrease	(0.25)	3,054	25,181
Expected Return ⁽²⁾ :			
Increase	0.25	(923)	
Decrease	(0.25)	923	

(1) The discount rate was 4.27% for 2017 expense and 3.75% for the projected benefit obligation at December 31, 2017.

(2) The expected return rate assumed was 6.96%.

The Company determines mortality assumptions through the use of published mortality tables that reflect broad-based studies of mortality and published longevity improvement scales.

The criteria used to determine the primary assumptions are discussed in *Note 9—Postretirement Benefits*. While we have used our best efforts to determine the most reliable assumptions, given the information available from company experience, economic data, independent consultants and other sources, we cannot be certain that actual results will be the same as expected. The assumptions are reviewed annually and revised, if necessary, based on more current information available to us. *Note 9—Postretirement Benefits* also contains information about pension plan assets, investment policies, and other related data.

CAUTIONARY STATEMENTS

We caution readers regarding certain forward-looking statements contained in the foregoing discussion and elsewhere in this document, and in any other statements made by us or on our behalf whether or not in future filings with the Securities and Exchange Commission. Any statement that is not a historical fact, or that might otherwise be considered an opinion or projection concerning us or our business, whether express or implied, is meant as and should be considered a forward-looking statement. Such statements represent our opinions concerning future operations, strategies, financial results or other developments.

Forward-looking statements are based upon estimates and assumptions that are subject to significant business, economic and competitive uncertainties, many of which are beyond our control. If these estimates or assumptions prove to be incorrect, the actual results may differ materially from the forward-looking statements made on the basis of such estimates or assumptions. Whether or not actual results differ materially from forward-looking statements may depend on numerous foreseeable and unforeseeable events or developments, which may be national in scope, related to the insurance industry generally, or applicable to Torchmark specifically. Such events or developments could include, but are not necessarily limited to:

- (1) Changes in lapse rates and/or sales of our insurance policies as well as levels of mortality, morbidity, and utilization of healthcare services that differ from our assumptions;
- (2) Federal and state legislative and regulatory developments, particularly those impacting taxes and changes to the federal Medicare program that would affect Medicare Supplement;
- (3) Market trends in the senior-aged health care industry that provide alternatives to traditional Medicare, such as health maintenance organizations (HMOs) and other managed care or private plans, and that could affect the sales of traditional Medicare Supplement insurance;
- (4) Interest rate changes that affect product sales and/or investment portfolio yield;
- (5) General economic, industry sector or individual debt issuers' financial conditions that may affect the current market value of securities that we own, or that may impair issuers' ability to pay interest due us on those securities;
- (6) Changes in pricing competition;
- (7) Litigation results;
- (8) Levels of administrative and operational efficiencies that differ from our assumptions;
- (9) Our inability to obtain timely and appropriate premium rate increases for health insurance policies due to regulatory delay;
- (10) The customer response to new products and marketing initiatives; and
- (11) Reported amounts in the financial statements which are based on our estimates and judgments which may differ from the actual amounts ultimately realized.

Readers are also directed to consider other risks and uncertainties described in our other documents on file with the Securities and Exchange Commission.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Information required by this item is found under the heading *Market Risk Sensitivity* in *Item 7* of this report.

Item 8. Financial Statements and Supplementary Data

Consolidated Financial Statements Index

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders and the Board of Directors of Torchmark Corporation (McKinney, Texas)

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Torchmark Corporation and subsidiaries (the "Company") as of December 31, 2017 and 2016, the related consolidated statements of operations, comprehensive income, shareholders' equity, and cash flows, for each of the three years in the period ended December 31, 2017, and the related notes and the schedules listed in the Index at Item 15 (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 26, 2018, expressed an unqualified opinion on the Company's internal control over financial reporting.

Basis for Opinion

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

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

/s/ DELOITTE & TOUCHE LLP

Dallas, Texas
February 26, 2018

We have served as the Company's auditor since 1999.

TORCHMARK CORPORATION
CONSOLIDATED BALANCE SHEETS
(Dollar amounts in thousands, except per share data)

	December 31,	
	2017	2016
Assets:		
Investments:		
Fixed maturities-available for sale, at fair value (amortized cost: 2017—\$14,995,101; 2016—\$14,188,050)	\$ 16,969,325	\$ 15,245,861
Policy loans	529,529	507,975
Other long-term investments	108,559	53,852
Short-term investments	127,071	72,040
Total investments	<u>17,734,484</u>	<u>15,879,728</u>
Cash	118,563	76,163
Accrued investment income	233,453	223,148
Other receivables	391,775	384,454
Deferred acquisition costs	3,958,063	3,783,158
Goodwill	441,591	441,591
Other assets	528,536	520,313
Assets related to discontinued operations	68,520	127,532
Total assets	<u>\$ 23,474,985</u>	<u>\$ 21,436,087</u>
Liabilities:		
Future policy benefits	\$ 13,439,472	\$ 12,825,837
Unearned and advance premiums	61,430	64,017
Policy claims and other benefits payable	333,294	299,565
Other policyholders' funds	97,635	96,993
Total policy liabilities	<u>13,931,831</u>	<u>13,286,412</u>
Current and deferred income taxes payable	1,312,002	1,743,990
Other liabilities	489,609	413,760
Short-term debt	328,067	264,475
Long-term debt (estimated fair value: 2017—\$1,228,392; 2016—\$1,233,019)	1,132,201	1,133,165
Liabilities related to discontinued operations	49,854	27,424
Total liabilities	<u>17,243,564</u>	<u>16,869,226</u>
Commitments and Contingencies (Note 15)		
Shareholders' equity:		
Preferred stock, par value \$1 per share—Authorized 5,000,000 shares; outstanding: 0 in 2017 and 2016	—	—
Common stock, par value \$1 per share—Authorized 320,000,000 shares; outstanding: (2017—124,218,183 issued, less 9,625,104 held in treasury and 2016—127,218,183 issued, less 9,187,075 held in treasury)	124,218	127,218
Additional paid-in capital	508,476	490,421
Accumulated other comprehensive income (loss)	1,424,274	577,574
Retained earnings	4,806,208	3,890,798
Treasury stock	(631,755)	(519,150)
Total shareholders' equity	<u>6,231,421</u>	<u>4,566,861</u>
Total liabilities and shareholders' equity	<u>\$ 23,474,985</u>	<u>\$ 21,436,087</u>

See accompanying Notes to Consolidated Financial Statements.

TORCHMARK CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollar amounts in thousands, except per share data)

	Year Ended December 31,		
	2017	2016	2015
Revenue:			
Life premium	\$ 2,306,547	\$ 2,189,333	\$ 2,073,065
Health premium	976,373	947,663	925,520
Other premium	15	38	135
Total premium	3,282,935	3,137,034	2,998,720
Net investment income	847,885	806,903	773,951
Realized investment gains (losses)	23,611	(10,683)	(8,791)
Other income	1,142	1,375	2,185
Total revenue	4,155,573	3,934,629	3,766,065
Benefits and expenses:			
Life policyholder benefits	1,558,261	1,479,272	1,374,608
Health policyholder benefits	633,778	612,725	602,610
Other policyholder benefits	35,836	36,751	38,994
Total policyholder benefits	2,227,875	2,128,748	2,016,212
Amortization of deferred acquisition costs	490,403	469,063	445,625
Commissions, premium taxes, and non-deferred acquisition expenses	264,860	249,174	237,541
Other operating expense	257,255	232,064	223,858
Interest expense	84,532	83,345	76,642
Total benefits and expenses	3,324,925	3,162,394	2,999,878
Income before income taxes	830,648	772,235	766,187
Income tax benefit (expense)	627,615	(232,645)	(249,894)
Income from continuing operations	1,458,263	539,590	516,293
Discontinued operations:			
Income (loss) from discontinued operations, net of tax	(3,769)	10,189	10,807
Net income	\$ 1,454,494	\$ 549,779	\$ 527,100
Basic net income per common share:			
Continuing operations	\$ 12.53	\$ 4.50	\$ 4.13
Discontinued operations	(0.03)	0.08	0.08
Total basic net income per common share	\$ 12.50	\$ 4.58	\$ 4.21
Diluted net income per common share:			
Continuing operations	\$ 12.26	\$ 4.41	\$ 4.07
Discontinued operations	(0.04)	0.08	0.09
Total diluted net income per common share	\$ 12.22	\$ 4.49	\$ 4.16

See accompanying Notes to Consolidated Financial Statements.

TORCHMARK CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollar amounts in thousands)

	Year Ended December 31,		
	2017	2016	2015
Net income	\$ 1,454,494	\$ 549,779	\$ 527,100
Other comprehensive income (loss):			
Unrealized investment gains (losses):			
Unrealized gains (losses) on securities:			
Unrealized holding gains (losses) arising during period	950,088	544,886	(1,163,417)
Reclassification adjustment for (gains) losses on securities included in net income	(34,954)	10,645	9,478
Reclassification adjustment for amortization of (discount) premium	(47)	(4,185)	(6,346)
Foreign exchange adjustment on securities recorded at fair value	1,326	312	(3,010)
Unrealized gains (losses) on securities	916,413	551,658	(1,163,295)
Unrealized gains (losses) on other investments:			
Unrealized holding gains (losses) arising during period	5,008	2,503	(1,635)
Reclassification adjustment for (gains) losses included in net income	—	(360)	(1,102)
Unrealized gains (losses) on other investments	5,008	2,143	(2,737)
Total unrealized investment gains (losses)	921,421	553,801	(1,166,032)
Less applicable (taxes) benefits	(322,553)	(193,820)	408,092
Unrealized gains (losses) on investments, net of tax	598,868	359,981	(757,940)
Unrealized gains (losses) attributable to deferred acquisition costs	(538)	(2,412)	8,682
Less applicable (taxes) benefits	188	845	(3,039)
Unrealized gains (losses) attributable to deferred acquisition costs, net of tax	(350)	(1,567)	5,643
Foreign exchange translation adjustments, other than securities	11,389	2,178	(20,651)
Less applicable (taxes) benefits	(2,937)	(838)	6,892
Foreign exchange translation adjustments, other than securities, net of tax	8,452	1,340	(13,759)
Pension adjustments:			
Amortization of pension costs	12,436	10,168	14,586
Plan amendments	—	—	(2,104)
Experience gain (loss)	(31,933)	(31,902)	(11,632)
Pension adjustments	(19,497)	(21,734)	850
Less applicable (taxes) benefits	6,827	7,607	(299)
Pension adjustments, net of tax	(12,670)	(14,127)	551
Other comprehensive income (loss)	594,300	345,627	(765,505)
Comprehensive income (loss)	\$ 2,048,794	\$ 895,406	\$ (238,405)

See accompanying Notes to Consolidated Financial Statements.

TORCHMARK CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Dollar amounts in thousands, except per share data)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock	Total Shareholders' Equity
Year Ended December 31, 2015							
Balance at January 1, 2015	\$ —	\$ 134,218	\$ 457,613	\$ 997,452	\$ 3,376,846	\$ (268,663)	\$ 4,697,466
Comprehensive income (loss)				(765,505)	527,100		(238,405)
Common dividends declared (\$.54 per share)					(67,182)		(67,182)
Acquisition of treasury stock						(418,526)	(418,526)
Stock-based compensation			21,813		(2,132)	8,983	28,664
Exercise of stock options			17,577		(36,322)	72,280	53,535
Retirement of treasury stock		(4,000)	(14,719)		(183,941)	202,660	—
Balance at December 31, 2015	—	130,218	482,284	231,947	3,614,369	(403,266)	4,055,552
Year Ended December 31, 2016							
Comprehensive income (loss)				345,627	549,779		895,406
Common dividends declared (\$.56 per share)					(66,968)		(66,968)
Acquisition of treasury stock						(404,784)	(404,784)
Stock-based compensation			19,659		(2,224)	8,891	26,326
Exercise of stock options					(53,845)	115,174	61,329
Retirement of treasury stock		(3,000)	(11,522)		(150,313)	164,835	—
Balance at December 31, 2016	—	127,218	490,421	577,574	3,890,798	(519,150)	4,566,861
Year Ended December 31, 2017							
Comprehensive income (loss)				594,300	1,454,494		2,048,794
Common dividends declared (\$.60 per share)					(69,494)		(69,494)
Acquisition of treasury stock						(412,989)	(412,989)
Stock-based compensation			30,190		(606)	7,450	37,034
Exercise of stock options					(38,333)	99,548	61,215
Reclassifications, Tax Reform ⁽¹⁾				252,400	(252,400)		—
Retirement of treasury stock		(3,000)	(12,135)		(178,251)	193,386	—
Balance at December 31, 2017	\$ —	\$ 124,218	\$ 508,476	\$ 1,424,274	\$ 4,806,208	\$ (631,755)	\$ 6,231,421

(1) Income tax effects of certain items were reclassified from accumulated other comprehensive income to retained earnings to remove stranded tax effects as a result of early adoption of ASU 2018-02, *Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. See further discussion in Note 1—Significant Accounting Policies.

See accompanying Notes to Consolidated Financial Statements.

TORCHMARK CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollar amounts in thousands)

	Year Ended December 31,		
	2017	2016	2015
Net income	\$ 1,454,494	\$ 549,779	\$ 527,100
Adjustments to reconcile net income from continuing operations to cash provided from continuing operations:			
Loss (Income) from discontinued operations, net of income taxes	3,769	(10,189)	(10,807)
Increase (decrease) in future policy benefits	687,407	645,844	631,202
Increase (decrease) in other policy benefits	31,784	24,668	14,609
Deferral of policy acquisition costs	(660,134)	(635,318)	(612,181)
Amortization of deferred policy acquisition costs	490,403	469,063	445,625
Change in current and deferred income taxes	(700,660)	152,210	103,558
Realized (gains) losses on sale of investments and properties	(23,611)	10,683	8,791
Other, net	67,933	20,079	13,985
Net cash provided from (used for) continuing operations	1,351,385	1,226,819	1,121,882
Net cash provided from (used for) discontinued operations	77,673	171,889	(1,832)
Cash provided from (used for) operating activities	1,429,058	1,398,708	1,120,050
Cash provided from (used for) investing activities:			
Investments sold or matured:			
Fixed maturities available for sale—sold	67,246	340,434	226,792
Fixed maturities available for sale—matured, called, and repaid	488,843	236,353	376,158
Other long-term investments	3,534	1,217	3,740
Total investments sold or matured	559,623	578,004	606,690
Acquisition of investments:			
Fixed maturities—available for sale	(1,314,609)	(1,530,053)	(1,070,908)
Other long-term investments	(55,096)	(20,444)	(31,707)
Total investments acquired	(1,369,705)	(1,550,497)	(1,102,615)
Net (increase) decrease in policy loans	(21,554)	(15,513)	(20,353)
Net (increase) decrease in short-term investments	(55,031)	(17,274)	(38,884)
Additions to properties	(20,285)	(25,162)	(36,957)
Sale of other assets	18	90	—
Investments in low-income housing interests	(19,890)	(32,084)	(41,231)
Cash provided from (used for) investing activities	(926,824)	(1,062,436)	(633,350)
Cash provided from (used for) financing activities:			
Issuance of common stock	61,215	61,329	35,958
Cash dividends paid to shareholders	(68,831)	(66,931)	(66,899)
Repayment of debt	(126,875)	(250,000)	—
Proceeds from issuance of debt	125,000	400,000	—
Payment for debt issuance costs	(1,661)	(9,638)	—
Net borrowing (repayment) of commercial paper	61,092	22,224	1,978
Excess tax benefit from stock option exercises	—	—	17,577
Acquisition of treasury stock	(412,989)	(404,784)	(418,526)
Net receipts (payments) from deposit-type product	(90,932)	(71,991)	(95,793)
Cash provided from (used for) financing activities	(453,981)	(319,791)	(525,705)
Effect of foreign exchange rate changes on cash	(5,853)	(1,701)	34,369
Increase (decrease) in cash	42,400	14,780	(4,636)
Cash at beginning of year	76,163	61,383	66,019
Cash at end of year	\$ 118,563	\$ 76,163	\$ 61,383

See accompanying Notes to Consolidated Financial Statements.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies

Business: Torchmark Corporation (Torchmark or alternatively, the Company) through its wholly-owned subsidiaries provides a variety of life and supplemental health insurance products and annuities to a broad base of customers. Torchmark is organized into four reportable segments: life insurance, health insurance, annuity, and investment.

Basis of Presentation: The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP), under guidance issued by the Financial Accounting Standards Board (FASB). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Principles of Consolidation: The consolidated financial statements include the results of Torchmark and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. When Torchmark acquires a subsidiary or a block of business, the assets acquired and the liabilities assumed are measured at fair value at the acquisition date. Any excess of acquisition cost over the fair value of net assets is recorded as goodwill. Expenses incurred to effect the acquisition are charged to earnings as of the acquisition date. Upon acquisition, the accounts and results of operations are consolidated as of and subsequent to the acquisition date.

Torchmark accounts for its variable interest entities (VIEs) under accounting guidance which clarifies the definition of a variable interest and the instructions for consolidating VIEs. Only primary beneficiaries are required or allowed to consolidate VIEs. Therefore, a company may have voting control of a VIE, but if it is not the primary beneficiary, it is not permitted to consolidate the VIE. As further described under the caption *Low-Income Housing Tax Credit Interests* below in this note, Torchmark holds passive interests in limited partnerships which provide investment returns through the provision of tax benefits (principally from the transfer of federal or state tax credits related to federal low-income housing). These interests are considered to be VIEs. They are not consolidated because the Company has no power to control the activities that most significantly affect the economic performance of these entities and therefore the Company is not the primary beneficiary of any of these interests. Torchmark's involvement is limited to its limited partnership interest in the entities. Torchmark has not provided any other financial support to the entities beyond its commitments to fund its limited partnership interests, and there are no arrangements or agreements with any of the interests to provide other financial support. The maximum loss exposure relative to these interests is limited to their carrying value.

Discontinued Operations: When a component of Torchmark's business is sold or expected to be sold during the ensuing year, Torchmark considers whether the criteria of ASC 205-20, *Discontinued Operations*, have been met, which includes evaluating if the disposal of a component represents a strategic shift that has, or will have, a major effect on the Company. If the disposal meets the criteria for discontinued operations, the assets and liabilities are segregated and recorded in the *Consolidated Balance Sheets* as "Assets and Liabilities related to discontinued operations" for all periods presented. If the carrying amount of the business exceeds its estimated fair value, a loss is recognized. The results of operations for the discontinued component are reported in "Income from discontinued operations, net of tax" in the *Consolidated Statements of Operations* for current and prior periods. Discontinued operations are reported commencing in the period in which the business is either disposed of or meets the accounting criteria for discontinued operations, including any gain or loss recognized on the sale or adjustment of the carrying amount to the estimated fair value less cost to sell.

As discussed in further detail in *Note 6—Discontinued Operations*, Torchmark sold one of its operating segments, Medicare Part D during 2016. The financial results of this business are excluded from Torchmark's continuing operations including the *Notes to the Consolidated Financial Statements*, other than *Note 2—Statutory Accounting* and *Note 6—Discontinued Operations*.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

Investments: Torchmark classifies all of its fixed maturity investments, which include bonds and redeemable preferred stocks, as available for sale. Investments classified as available for sale are carried at fair value with unrealized gains and losses, net of deferred taxes, reflected directly in accumulated other comprehensive income. Policy loans are carried at unpaid principal balances. Other long-term investments include equity securities, real estate, mortgage participations, and limited partnerships. Investments in equity securities, which include common and nonredeemable preferred stocks, are reported at fair value with unrealized gains and losses, net of deferred taxes, reflected directly in accumulated other comprehensive income. Investments in real estate are reported at cost less allowances for depreciation. Depreciation is calculated on the straight-line method. Mortgage participations, a type of investment where the mortgage loan is shared among investors, are accounted for as financing receivables. Investments in limited partnerships are primarily accounted for using the cost method of accounting as Torchmark's partnership interest is minor as Torchmark lacks the ability to exercise significant influence over the partnership's operating and financial policies. The Company considers its cost method investments for impairment when the carrying value of such investments exceeds the net asset value ("NAV"). As further discussed below in *Accounting Pronouncements Not Yet Adopted*, the Company will adopt ASU 2016-01 on January 1, 2018 which removes the cost method for certain investments and replaces it with fair value through net income method. Under the new guidance, limited partnerships will be reported at fair value and all fluctuations in fair value will be reported through realized gains and losses. Short-term investments include investments in interest-bearing assets with original maturities of twelve months or less. Gains and losses realized on the disposition of investments are determined on a specific identification basis.

Fair Value Measurements, Investments in Securities: Torchmark measures the fair value of its fixed maturities based on a hierarchy consisting of three levels which indicate the quality of the fair value measurements as described below:

- *Level 1*—fair values are based on quoted prices in active markets for identical assets or liabilities that the Company has the ability to access as of the measurement date.
- *Level 2*—fair values are based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or inputs that can otherwise be corroborated by observable market data.
- *Level 3*— fair values are based on inputs that are considered unobservable where there is little, if any, market activity for the asset or liability as of the measurement date. In this circumstance, the Company has to rely on values derived by independent brokers or internally-developed assumptions. Unobservable inputs are developed based on the best information available to the Company which may include the Company's own data or bid and ask prices in the dealer market.

The great majority of Torchmark's fixed maturities are not actively traded and direct quotes are not generally available. Management therefore determines the fair values of these securities after consideration of data provided by third-party pricing services, independent broker/dealers, and other resources. At December 31, 2017, Torchmark's investments in fixed maturities were primarily composed of the following significant security types: Corporate securities, state and municipal securities, redeemable preferred stocks, and U.S. government securities. The remaining security types represented less than 1% of the total in the aggregate.

Over 95% of the fair value reported at December 31, 2017 was determined using data provided by third-party pricing services. Prices provided by these services are not binding offers, but are estimated exit values. Third-party pricing services use proprietary pricing models to determine security values by discounting cash flows using a market-adjusted spread to a benchmark yield.

For all asset classes within Torchmark's significant security types, third-party pricing services use a common valuation technique to model the price of the investments using observable market data. The foundation for these models consists of developing yield spreads based on multiple observable market inputs, including but not limited to: benchmark yield curves, actual trading activity, new issue yields, broker-dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, sector-specific data, economic data, and other inputs that are corroborated in the market. Pricing

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

vendors monitor and review their pricing data continuously with current market and economic data feeds, augmented by ongoing communication within the dealer community.

Using the observable market inputs described above, spreads to an appropriate benchmark yield are further developed by the vendors for each security based on security-specific and/or sector-specific risk factors, such as a security's terms and conditions (coupon, maturity, and call features), credit rating, sector, liquidity, collateral or other cash flow options, and other factors that could impact the risk of the security. Embedded repayment options, such as call and redemption features, are also taken into account in the pricing models. When the spread is determined, it is added to the security's benchmark yield. The security's expected cash flows are discounted using this spread-adjusted yield, and the resulting present value of the discounted cash flows is the evaluated price.

When third-party vendor prices are not available, the Company attempts to obtain valuations from other sources, including but not limited to broker/dealers, broker quotes, and prices on comparable securities.

When valuations have been obtained for all securities in the portfolio, management reviews and analyzes the prices to ensure their reasonableness, taking into account available observable information. When two or more valuations are available for a security and the variance between the prices is 10% or less, the close correlation suggests similar observable inputs were used in deriving the price, and the mean of the prices is used. Securities valued in this manner are classified as Level 2. When the variance between two or more valuations for a security exceeds 10%, additional analysis is performed to determine the most appropriate value for that security, using resources such as broker quotes, prices on comparable securities, recent trades, and any other observable market data. Further review is performed on the available valuations to determine if they can be corroborated within reasonable tolerance to any other observable evidence. If one of the valuations or the mean of the available valuations for a security can be corroborated with other observable evidence, then the corroborated value is used and reported as Level 2. The Company uses information and analytical techniques deemed appropriate for determining the point within the range of reasonable fair value estimates that is most representative of fair value under current market conditions. Valuations that cannot be corroborated within a reasonable tolerance are classified as Level 3.

Torchmark invests in a portfolio of private placement bonds which are not actively traded. This portfolio is managed by third parties. The portfolio managers provide valuations for the bonds based on a pricing matrix utilizing observable inputs, such as the benchmark treasury rate and published sector indices, and unobservable inputs such as an internally-developed credit rating. If they cannot be corroborated, the fair values are classified as Level 3.

The fair values for each class of security and by valuation hierarchy level are indicated in *Note 4—Investments* under the caption *Fair value measurements* and *Note 9—Postretirement Benefits* under the caption *Pension Plans*.

Fair Value Measurements, Other Financial Instruments: Fair values for cash, short-term investments, short-term debt, mortgage participations, receivables and payables approximate carrying value. Policy loans are an integral part of Torchmark's subsidiaries' life insurance policies in force and their fair values cannot be valued separately and apart from the insurance contracts. The fair values of Torchmark's long-term debt issues are based on the same methodology as investments in fixed maturities. At December 31, 2017, observable inputs were available for these debt securities and as such were classified as Level 2 in the valuation hierarchy. The fair value for each debt instrument as of December 31, 2017 is disclosed in *Note 11—Debt*. As described in *Note 9—Postretirement Benefits*, Torchmark maintains a nonqualified supplemental retirement plan. Therefore the assets which support the liability for this plan are considered general assets of the Company. These assets consist of the cash value of corporate-owned life insurance policies (COLI) and exchange traded funds (ETFs). The fair value of the insurance cash values approximates carrying value. Fair values for the ETFs are derived from direct quotes and are considered Level 1 in the valuation hierarchy.

Impairment of Investments: Torchmark's portfolio of fixed maturities fluctuates in value due to changes in interest rates in the financial markets as well as other factors. Fluctuations caused by market interest rate changes have little bearing on whether or not the investment will be ultimately recoverable. Therefore, Torchmark considers these declines in value resulting from changes in market interest rates to be temporary. In certain circumstances, however, Torchmark determines that the decline in the value of a security is other-than-temporary and writes the book value of the security

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

down to its fair value, realizing an investment loss. The evaluation of Torchmark's securities for other-than-temporary impairments is a process that is undertaken at least quarterly and is overseen by a team of investment and accounting professionals. Each security, which is impaired because the fair value is less than the cost or amortized cost, is identified and evaluated. The determination that an impairment is other-than-temporary is highly subjective and involves the careful consideration of many factors. Among the factors considered are:

- The length of time and extent to which the security has been impaired
- The reason(s) for the impairment
- The financial condition of the issuer and the prospects for recovery in fair value of the security
- The Company's ability and intent to hold the security until anticipated recovery
- Expected future cash flows

The relative weight given to each of these factors can change over time as facts and circumstances change. In many cases, management believes it is appropriate to give relatively more weight to prospective factors than to retrospective factors. Prospective factors that are given more weight include prospects for recovery, the Company's ability and intent to hold the security until anticipated recovery, and expected future cash flows.

Among the facts and information considered in the process are:

- Financial statements of the issuer
- Changes in credit ratings of the issuer
- The value of underlying collateral
- News and information included in press releases issued by the issuer
- News and information reported in the media concerning the issuer
- News and information published by or otherwise provided by credit analysts
- The nature and amount of recent and expected future sources and uses of cash
- Default on a required payment
- Issuer bankruptcy filings

While all available information is taken into account, it is difficult to predict the ultimate recoverable amount of a distressed or impaired security. If a security is determined to be other-than-temporarily impaired, the cost basis of the security is written down to fair value and is treated as a realized loss in the period the determination is made. The written-down security will be amortized and revenue recognized in accordance with estimated future cash flows.

Current accounting guidance is such that if an entity intends to sell or if it is more likely than not that it will be required to sell an impaired security prior to recovery of its cost basis, the security is to be considered other-than-temporarily impaired and the full amount of impairment must be charged to earnings. Otherwise, losses on fixed maturities which are other-than-temporarily impaired are separated into two categories, the portion of loss which is considered credit loss and the portion of loss which is due to other factors. The credit loss portion is charged to earnings while the loss due to other factors is charged to other comprehensive income. The credit loss portion of an impairment is determined as the difference between the security's amortized cost and the present value of expected future cash flows discounted at the security's original effective yield rate. The temporary portion is the difference between this present value of expected future cash flows and fair value (as discounted by a market yield). The expected cash flows are determined using judgment and the best information available to the Company. Inputs used to derive expected cash flows include expected default rates, current levels of subordination, and loan-to-collateral value ratios.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

Cash: Cash consists of balances on hand and on deposit in banks and financial institutions.

Accrued investment income: Accrued investment income consists of interest income or dividends earned on the investment portfolio, but are yet to be received as of the balance sheet date.

Other Receivables: Other receivables consist mostly of agent debit balances, which primarily represent commissions advanced to insurance agents. These balances are repaid to the Company over time as the premiums associated with the advanced commissions are collected by the Company and the agents' commissions on such premiums are retained. The balances were \$378 million and \$353 million at December 31, 2017 and 2016, respectively. Management believes these balances are recoverable as they are less than the estimated present value of future commissions.

Deferred Acquisition Costs: Certain costs of acquiring new insurance business are deferred and recorded as an asset. These costs are essential for the acquisition of new insurance business and are directly related to the successful issuance of an insurance contract including sales commissions, policy issue costs, and underwriting costs. Additionally, deferred acquisition costs (DAC) include the value of business acquired (VOBA), which are the costs of acquiring blocks of insurance from other companies or through the acquisition of other companies. These costs represent the difference between the fair value of the contractual insurance assets acquired and liabilities assumed compared against the assets and liabilities for insurance contracts that the Company issues or holds measured in accordance with GAAP.

DAC and VOBA are amortized in a systematic manner which matches these costs with the associated revenues. Policies other than universal life-type policies are amortized with interest over the estimated premium-paying period of the policies in a manner which charges each year's operations in proportion to the receipt of premium income. Universal life-type policies are amortized with interest in proportion to estimated gross profits. The assumptions used to amortize acquisition costs with regard to interest, mortality, morbidity, and persistency are consistent with those used to estimate the liability for future policy benefits. For interest-sensitive and deposit-balance type products, these assumptions are reviewed on a regular basis and are revised if actual experience differs significantly from original expectations. For all other products, amortization assumptions are generally not revised once established.

DAC are subject to periodic recoverability and loss recognition testing to determine if there is a premium deficiency. These tests evaluate whether the present value of future contract-related cash flows will support the capitalized DAC asset. These cash flows consist primarily of premium income, less benefits and expenses taking inflation into account. The present value of these cash flows, less the benefit reserve, is then compared with the unamortized deferred acquisition cost balance. In the event the estimated present value of net cash flows is less, the deficiency would be recognized by a charge to earnings and either a reduction of unamortized acquisition costs or an increase in the liability for future benefits, as described under the caption *Future Policy Benefits*.

Advertising Costs: Costs related to advertising are generally charged to expense as incurred. However, certain Globe Life Direct Response advertising costs are capitalized when there is a reliable and demonstrated relationship between total costs and future benefits that is a direct result of incurring these costs. Globe Life Direct Response advertising costs consist primarily of the production and distribution costs of direct mail advertising materials, and when capitalized are included as a component of DAC. They are amortized in the same manner as other DAC. Globe Life Direct Response advertising costs charged to earnings and included in other operating expense were \$9.3 million, \$9.3 million, and \$9.7 million in 2017, 2016, and 2015, respectively. At December 31, 2017, unamortized capitalized advertising costs included within DAC were \$1.28 billion at December 31, 2017 and \$1.25 billion at December 31, 2016.

Goodwill: The excess cost of a business acquired over the fair value of net assets acquired is reported as goodwill. Goodwill is subject to impairment testing in accordance with GAAP on an annual basis, or whenever potential impairment triggers occur. The Company may perform a qualitative analysis under certain circumstances, or perform a two-step quantitative analysis. In the qualitative analysis, the Company determines if it is more likely than not that the fair value of a reporting unit is less than its carrying amount by assessing current events and circumstances. If there are factors present indicating potential impairment, the Company would proceed to the two-step quantitative analysis.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

In the two-step quantitative analysis, the Company utilizes two approaches, income and market, to determine the fair value of each reporting unit. In the income approach, judgment and assumptions are used in developing the projected cash flows for the reporting units, and such estimates are subject to change. The Company also exercises judgment in the determination of the discount rate as management believes this to be appropriate for the risk associated with the cash flow expectations. In the market approach, the Company utilizes the share price and a control premium based on businesses with similar assets to determine a fair value. In both cases, the fair value of each reporting unit is then measured against that reporting unit's corresponding carrying value. In the event the fair value is less than the carrying value, further testing is required under the accounting guidance to determine the amount of impairment, if any. If there is an impairment in the goodwill of any reporting unit, it is written down and charged to earnings in the period of the test.

Torchmark tested its goodwill annually as of June 30th in each of the years 2015 through 2017. Torchmark's goodwill was not impaired in any of those periods.

Low-Income Housing Tax Credit Interests: Torchmark invests in limited partnerships that provide low-income housing tax credits and other related federal income tax benefits to Torchmark. The carrying value of Torchmark's investment in these entities was \$228 million and \$280 million at December 31, 2017 and 2016, respectively and was included in "Other assets" on the *Consolidated Balance Sheets*. As of December 31, 2017, Torchmark was obligated under future commitments of \$34 million, which are recorded in "Other liabilities". For guaranteed investments acquired prior to January 1, 2015, the Company utilizes the effective-yield method of amortization while the proportional method of amortization is utilized for all non-guaranteed as well as guaranteed investments acquired on or after January 1, 2015. All amortization expense is recorded in "Income tax benefit (expense)" on the *Consolidated Statements of Operations*.

Property and Equipment: Property and equipment, included in "Other assets," is reported at cost less allowances for depreciation. Depreciation is recorded primarily on the straight line method over the estimated useful lives of these assets which range from three to five years for equipment and ten to forty years for buildings and improvements. Ordinary maintenance and repairs are charged to income as incurred. Impairments, if any, are recorded when certain events and circumstances become evident that the fair value of the asset is less than its carrying amount. Original cost of property and equipment was \$217 million at December 31, 2017 and \$196 million at December 31, 2016. Accumulated depreciation was \$109 million at year end 2017 and \$99 million at the end of 2016. Depreciation expense was \$10.5 million in 2017, \$9.8 million in 2016, and \$8.0 million in 2015. Internally generated software costs are expensed as incurred in the preliminary project phase and post-implementation phase, and will be capitalized during the application development stage.

Future Policy Benefits: The liability for future policy benefits for annuity and universal life-type products is represented by policy account value. The liability for future policy benefits for all other life and health products, approximately 87% of total future policy benefits, is determined on the net level premium method. This method provides for the present value of expected future benefit payments less the present value of expected future net premiums, based on estimated investment yields, mortality, morbidity, persistency and other assumptions which were considered appropriate at the time the policies were issued. For limited-payment contracts, a deferred profit liability is also recorded which causes profits to emerge over the life of the contract in proportion to policies in force.

Assumptions used for traditional life and health insurance products are based primarily on Company experience. Assumptions for interest rates range from 2.5% to 7.0% for Torchmark's insurance companies with an overall weighted average assumed rate of 5.80%. Mortality tables used for individual life insurance include various statutory tables and modifications of a variety of generally accepted actuarial tables. Morbidity assumptions for individual health are based on Company experience and industry data. Withdrawal and termination assumptions are based on Torchmark's experience. Once established, assumptions for these products are generally not changed. An additional provision is made on most products to allow for possible adverse deviation from the assumptions. These estimates are reviewed annually and compared with actual experience. If it is determined that existing contract liabilities, together with the present value of future gross premiums, will not be sufficient to cover the present value of future benefits and to recover unamortized deferred acquisition costs, then a premium deficiency exists. Such a deficiency would be recognized

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

immediately by a charge to earnings and either a reduction of unamortized deferred acquisition costs or an increase in the liability for future policy benefits. From that point forward, the liability for future policy benefits would be based on revised assumptions.

Policy Claims and Other Benefits Payable: Torchmark establishes a liability for known policy benefits payable and an estimate of claims that have been incurred but not yet reported to the Company. Torchmark makes an estimate of unreported claims after careful evaluation of all information available to the Company. This estimate is based on prior experience and is reviewed quarterly. However, there is no certainty the stated liability for claims and other benefits, including the estimate of unsubmitted claims, will be Torchmark's ultimate obligation.

Income Taxes: Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement book values and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

On December 22, 2017, the Tax Cuts and Jobs Act (Tax Legislation) was enacted into law which changed existing tax law, including a reduction of the corporate income tax rate from 35% to 21% effective January 1, 2018. The Company recorded \$877 million of tax benefits in net income in 2017 as a result of re-measuring its deferred assets and liabilities using the lower corporate tax rate as of the date of enactment. Based on the analysis of the Tax Legislation, the Company was able to determine that this amount is a reasonable estimate of the impact of the Tax Legislation in accordance with SEC Staff Accounting Bulletin (SAB) No. 118. However, the Company will continue to analyze relevant information to complete the accounting for income taxes which may result in an adjustment to tax expense in 2018. The accounting is expected to be complete when the 2017 U.S. corporate income tax returns are filed later in 2018. More information concerning income taxes is provided in *Note 8—Income Taxes*.

Postretirement Benefits: Torchmark accounts for its postretirement defined benefit plans by recognizing the funded status of those plans on its *Consolidated Balance Sheets* in accordance with accounting guidance. Periodic gains and losses attributable to changes in plan assets and liabilities that are not recognized as components of net periodic benefit costs are recognized as components of other comprehensive income, net of tax. More information concerning the accounting and disclosures for postretirement benefits is found in *Note 9—Postretirement Benefits*.

Treasury Stock: Torchmark accounts for purchases of treasury stock on the cost method. Issuance of treasury stock is accounted for using the weighted-average cost method. More information is found in *Note 12—Shareholders' Equity*.

Recognition of Premium Revenue and Related Expenses: Premium income for traditional long-duration life and health insurance products is recognized evenly over the contract period and when due from the policyholder. Premiums for short-duration health contracts are recognized as revenue over the contract period in proportion to the insurance protection provided. Premiums for universal life-type and annuity contracts are added to the policy account value, and revenues for such products are recognized as charges to the policy account value for mortality, administration, and surrenders (retrospective deposit method). Life premium includes policy charges of \$17 million, \$18 million, and \$19 million for the years ended December 31, 2017, 2016, and 2015, respectively. Other premium consists of annuity policy charges in each year. For most insurance products, the related benefits and expenses are matched with revenues by means of the provision of future policy benefits and the amortization of DAC in a manner which recognizes profits as they are earned over the revenue recognition period. For limited-payment life insurance products, the profits are recognized over the contract period.

Stock-Based Compensation: Torchmark accounts for stock-based compensation by recognizing an expense in the financial statements based on the "fair value method." The fair value method requires that a fair value be assigned to a stock option or other stock grant on its grant date and that this value be amortized over the grantees' service period.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

The fair value method requires the use of an option valuation model to value employee stock options. Torchmark has elected to use the Black-Scholes valuation model for option expensing. A summary of assumptions for options granted in each of the three years 2015 through 2017 is as follows:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Volatility factor	14.8%	19.2%	23.6%
Dividend yield	0.7%	1.1%	0.9%
Expected term (in years)	5.71	5.78	5.66
Risk-free rate	2.0%	1.3%	1.6%

The expected term is generally derived from Company experience. However, expected terms are determined based on the simplified method as permitted under the ASC 718 *Stock Compensation* topic when Company experience is insufficient. The Torchmark Corporation 2011 Incentive Plan replaced all previous plans and allows for option grants for employees with a ten-year contractual term which vest over five years in addition to seven-year grants which vest over three years as permitted by the previous plans. Director grants vest over six months. The Company has sufficient experience with seven-year grants that vest in three years, but insufficient historical experience with five-year vesting. Therefore, Torchmark has used the simplified method to determine the expected term for the ten-year grants with five-year vesting and will do so until adequate experience is developed. Volatility and risk-free interest rates are assumed over a period of time consistent with the expected term of the option. Volatility is measured on a historical basis. Monthly data points are utilized to derive volatility for periods greater than three years. Expected dividend yield is based on current dividend yield held constant over the expected term. Once the fair value of an option has been determined, it is amortized on a straight-line basis over the employee’s service period for that grant (from the grant date to the date the grant is fully vested). Expenses for restricted stock and restricted stock units are based on the grant date fair value allocated on a straight-line basis over the service period. Performance share expense is recognized based on management’s estimate of the probability of meeting the metrics identified in the performance share award agreement, assigned to each service period as these estimates develop.

Torchmark management views all stock-based compensation expense as a corporate or Parent Company expense and, therefore, presents it as such in its segment analysis (See *Note 14—Business Segments*). It is included in “Other operating expense” in the *Consolidated Statements of Operations*.

Earnings Per Share: Torchmark presents basic and diluted earnings per common share (EPS) on the face of the *Consolidated Statements of Operations* for income from continuing operations and income from discontinued operations. Basic EPS is computed by dividing income available to common shareholders by the weighted average common shares outstanding for the period. Diluted EPS is calculated by adding to shares outstanding the additional net effect of potentially dilutive securities or contracts, such as stock options, which could be exercised or converted into common shares. For more information on earnings per share, see *Note 12—Shareholders’ Equity*.

Accounting Pronouncements Adopted in the Current Year:

ASU 2018-02: In February 2018, the FASB issued ASU No. 2018-02, *Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income (AOCI)*. This guidance was issued to allow the reclassification of taxes from AOCI to retained earnings as a result of the reduction in corporate income tax rates due to Tax Legislation. Current accounting requires the effect of changes in tax rates used to measure deferred tax assets and liabilities to be reported in net income as of the date of enactment even though deferred taxes were previously recognized in AOCI (stranded taxes). This guidance, however, allows a company to elect to reclassify the stranded taxes in AOCI to retained earnings and is effective for years beginning after December 15, 2018, with early adoption permitted. The Company elected to early adopt this guidance resulting in a reclassification of \$252 million from AOCI to retained earnings for the period ended December 31, 2017. See *Consolidated Statements of Shareholders’ Equity* and *Note 3—Supplemental Information about Changes to Accumulated Other Comprehensive Income*.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

Accounting Pronouncements Not Yet Adopted:

ASU 2016-01: In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, which primarily revises the classification and measurement of certain equity investments such that they will be measured at fair value through net income. Additionally, it eliminates the cost method for partnerships and joint ventures and requires these types of investments to be accounted for under the fair value through net income method or equity method. Lastly, the guidance will require certain disclosures associated with fair value of financial instruments. This standard became effective for the Company on January 1, 2018. The adoption will result in a \$6 million positive adjustment to the opening balance of retained earnings as we have minimal ownership interests in equity investments and partnerships.

ASU 2016-02: In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which requires all lessees to report a right-of-use asset and a lease liability for leases with a term life greater than 12 months. Operating and financing leases will be recognized on the balance sheet going forward. Additional qualitative and quantitative disclosures will be required. This standard will become effective for the Company beginning January 1, 2019 and will require recognizing and measuring leases at the beginning of the earliest period presented using a modified retrospective approach. Early adoption is permitted. The Company does not expect the adoption to have a significant impact on the financial statements. Refer to *Note 15—Commitments and Contingencies* for consideration of the noncancelable operating lease commitments. The Company is not a lessor.

ASU 2016-13: In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments as well as to change the loss impairment methodology for available-for-sale debt securities by use of an allowance rather than a direct write-down. This standard will become effective on January 1, 2020. The applicable section of the standard related to debt securities requires a prospective transition. The Company does not expect the adoption to have a significant impact on the financial statements as we have limited credit losses with respect to our available-for-sale portfolio.

ASU 2016-15: In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* to provide uniformity in the classification of cash receipts and payments recorded in the statement of cash flows including debt prepayment or debt extinguishment costs, settlement of zero-coupon bonds, and proceeds from the settlement of insurance claims. This standard became effective on January 1, 2018 and will not have a significant impact to the classification on our *Statement of Cash Flows*.

ASU 2016-16: In October 2016, the FASB issued ASU No. 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfer of Assets Other Than Inventory*. This guidance was issued to improve the accounting for income tax consequences of intra-entity transfers of assets other than inventory by allowing the immediate recognition of the current and deferred income tax effects. Current guidance prohibits the recognition of current and deferred income taxes for an intra-entity transfer until the asset has been sold to an outside party. This new guidance should be applied on a modified retrospective approach and became effective on January 1, 2018. This adoption will not have a significant impact on the financial statements.

ASU 2017-04: In January 2017, the FASB issued ASU No. 2017-04, *Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*. This guidance was issued to simplify the subsequent measurement of goodwill through the elimination of Step 2 from the goodwill impairment test which required a hypothetical purchase price allocation. It will become effective on January 1, 2020 and should be applied on a prospective basis. This adoption will not have an impact to the financial statements.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 1—Significant Accounting Policies (continued)

ASU 2017-07: In March 2017, the FASB issued ASU No. 2017-07, *Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This guidance was issued to simplify the reporting of pension costs by disaggregating the service-cost component from the other components of net benefit costs and reporting it separately on the income statement. The service-cost component is the only component of net benefit cost that will be eligible for capitalization. The guidance became effective on January 1, 2018 with a retrospective transition method for separation of net benefit costs and a prospective transition method for the capitalization of service costs. The Company expects the adoption to add an additional \$3 to \$5 million in expense to the 2018 *Consolidated Statements of Operations* due to the elimination of the ability to capitalize a portion of the benefit costs.

ASU 2017-08: In March 2017, the FASB issued ASU No. 2017-08, *Receivables—Nonrefundable Fees and Other Costs (Topic 310-20): Premium Amortization on Purchased Callable Debt Securities*. This guidance was issued to shorten the amortization period for certain callable debt securities held at a premium. The guidance requires the premium to be amortized to the earliest call date. It will become effective on January 1, 2019 with early adoption permitted, including during interim periods. The adoption is to be applied on a modified retrospective basis through an adjustment to retained earnings. This adoption will not have a significant impact on the financial statements.

ASU 2017-09: In May 2017, the FASB issued ASU No. 2017-09, *Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting*. This guidance was issued to provide clarity and guidance regarding changes to the terms or conditions of a share-based payment award that requires an entity to apply modification accounting. It became effective on January 1, 2018 with early adoption permitted, including adoption in any interim periods. The adoption will have a minimal impact on the financial statements as modifications to stock compensation are infrequent.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 2—Statutory Accounting

Life insurance subsidiaries of Torchmark are required to file statutory financial statements with state insurance regulatory authorities. Accounting principles used to prepare these statutory financial statements differ from GAAP. Consolidated net income and shareholders' equity (capital and surplus) on a statutory basis for the insurance subsidiaries were as follows:

	Net Income			Shareholders' Equity	
	Year Ended December 31,			At December 31,	
	2017	2016	2015	2017	2016
Life insurance subsidiaries	\$ 426,285	\$ 429,563	\$ 393,466	\$ 1,254,875	\$ 1,335,070

The excess, if any, of shareholder's equity of the insurance subsidiaries on a GAAP basis over that determined on a statutory basis is not available for distribution by the insurance subsidiaries to Torchmark without regulatory approval. Insurance subsidiaries' statutory capital and surplus necessary to satisfy regulatory requirements in the aggregate was \$458 million at December 31, 2017. More information on the restrictions on the payment of dividends can be found in *Note 12—Shareholders' Equity*.

Torchmark's statutory financial statements are presented on the basis of accounting practices prescribed by the insurance department of the state of domicile of each insurance subsidiary. While all states have adopted the National Association of Insurance Commissioners' (NAIC) statutory accounting practices (NAIC SAP) as the basis for statutory accounting, certain states have retained prescribed practices of their respective insurance code or administrative code which can differ from NAIC SAP. For Torchmark's life insurance companies, there are no significant differences between NAIC SAP and the accounting practices prescribed by the states of domicile.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 3—Supplemental Information about Changes to Accumulated Other Comprehensive Income

An analysis in the change in balance by component of Accumulated Other Comprehensive Income is as follows for each of the years 2015 through 2017.

Components of Accumulated Other Comprehensive Income

For the 12 months ended December 31, 2015:	Available for Sale Assets	Deferred Acquisition Costs	Foreign Exchange	Pension Adjustments	Total
Balance at January 1, 2015	\$ 1,090,273	\$ (10,758)	\$ 17,386	\$ (99,449)	\$ 997,452
Other comprehensive income (loss) before reclassifications, net of tax	(759,976)	5,643	(13,759)	(8,930)	(777,022)
Reclassifications, net of tax	2,036	—	—	9,481	11,517
Other comprehensive income (loss)	<u>(757,940)</u>	<u>5,643</u>	<u>(13,759)</u>	<u>551</u>	<u>(765,505)</u>
Balance at December 31, 2015	332,333	(5,115)	3,627	(98,898)	231,947
For the 12 months ended December 31, 2016:					
Other comprehensive income (loss) before reclassifications, net of tax	356,016	(1,567)	1,340	(20,736)	335,053
Reclassifications, net of tax	3,965	—	—	6,609	10,574
Other comprehensive income (loss)	<u>359,981</u>	<u>(1,567)</u>	<u>1,340</u>	<u>(14,127)</u>	<u>345,627</u>
Balance at December 31, 2016	692,314	(6,682)	4,967	(113,025)	577,574
For the 12 months ended December 31, 2017:					
Other comprehensive income (loss) before reclassifications, net of tax	621,619	(350)	8,452	(20,753)	608,968
Reclassifications, net of tax	(22,751)	—	—	8,083	(14,668)
Other comprehensive income (loss)	<u>598,868</u>	<u>(350)</u>	<u>8,452</u>	<u>(12,670)</u>	<u>594,300</u>
Reclassifications, Tax reform ⁽¹⁾	278,107	(1,515)	2,883	(27,075)	252,400
Balance at December 31, 2017	<u>\$ 1,569,289</u>	<u>\$ (8,547)</u>	<u>\$ 16,302</u>	<u>\$ (152,770)</u>	<u>\$ 1,424,274</u>

(1) Income tax effects of certain items were reclassified from accumulated other comprehensive income to retained earnings to remove stranded tax effects as a result of early adoption of ASU No. 2018-02, *Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. See further discussion in Note 1—*Significant Accounting Policies*.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 3—Supplemental Information about Changes to Accumulated Other Comprehensive Income (continued)

Reclassification adjustments out of Accumulated Other Comprehensive Income are presented below for each of the years 2015 through 2017.

Reclassification Adjustments

Component Line Item	Year Ended December 31,			Affected line items in the Statement of Operations
	2017	2016	2015	
Unrealized gains (losses) on available for sale assets:				
Realized (gains) losses	\$ (34,954)	\$ 10,285	\$ 9,478	Realized investment gains (losses)
Amortization of (discount) premium	(47)	(4,185)	(6,346)	Net investment income
Total before tax	(35,001)	6,100	3,132	
Tax	12,250	(2,135)	(1,096)	Income taxes
Total after tax	(22,751)	3,965	2,036	
Pension adjustments:				
Amortization of prior service cost	476	477	377	Other operating expenses
Amortization of actuarial (gain) loss	11,960	9,691	14,209	Other operating expenses
Total before tax	12,436	10,168	14,586	
Tax	(4,353)	(3,559)	(5,105)	Income taxes
Total after tax	8,083	6,609	9,481	
Total reclassifications (after tax)	<u>\$ (14,668)</u>	<u>\$ 10,574</u>	<u>\$ 11,517</u>	

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments

Portfolio Composition:

A summary of fixed maturities available for sale by cost or amortized cost and estimated fair value at December 31, 2017 and 2016 is as follows:

2017:	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value⁽¹⁾	% of Total Fixed Maturities⁽²⁾
Fixed maturities available for sale:					
U.S. Government direct, guaranteed, and government-sponsored enterprises	\$ 390,646	\$ 18,173	\$ (1,373)	\$ 407,446	2
States, municipalities, and political subdivisions	1,091,960	127,890	(135)	1,219,715	7
Foreign governments	20,236	1,782	—	22,018	—
Corporates, by sector:					
Financial	3,282,526	475,961	(23,392)	3,735,095	22
Utilities	1,955,737	369,406	(1,298)	2,323,845	14
Energy	1,619,349	226,140	(25,392)	1,820,097	11
Other corporate sectors	6,065,803	747,612	(20,616)	6,792,799	40
Total corporates	12,923,415	1,819,119	(70,698)	14,671,836	87
Collateralized debt obligations	59,150	20,084	(7,653)	71,581	—
Other asset-backed securities	144,520	4,835	—	149,355	1
Redeemable preferred stocks, by sector:					
Financial	336,621	62,892	(2,727)	396,786	3
Utilities	28,553	2,132	(97)	30,588	—
Total redeemable preferred stocks	365,174	65,024	(2,824)	427,374	3
Total fixed maturities	\$14,995,101	\$ 2,056,907	\$ (82,683)	\$ 16,969,325	100

(1) Amount reported in the balance sheet.

(2) At fair value.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

2016:	<u>Cost or Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value⁽¹⁾</u>	<u>% of Total Fixed Maturities⁽²⁾</u>
Fixed maturities available for sale:					
U.S. Government direct, guaranteed, and government-sponsored enterprises	\$ 381,054	\$ 895	\$ (9,151)	\$ 372,798	3
States, municipalities, and political subdivisions	1,284,605	126,850	(1,327)	1,410,128	9
Foreign governments	21,701	1,438	(62)	23,077	—
Corporates, by sector:					
Financial	2,963,584	285,037	(45,885)	3,202,736	21
Utilities	1,875,946	249,701	(12,604)	2,113,043	14
Energy	1,542,426	127,989	(44,324)	1,626,091	11
Other corporate sectors	5,601,136	424,021	(84,547)	5,940,610	39
Total corporates	11,983,092	1,086,748	(187,360)	12,882,480	85
Collateralized debt obligations	60,726	13,062	(10,285)	63,503	—
Other asset-backed securities	56,410	621	(337)	56,694	—
Redeemable preferred stocks, by sector:					
Financial	371,862	43,383	(7,218)	408,027	3
Utilities	28,600	798	(244)	29,154	—
Total redeemable preferred stocks	400,462	44,181	(7,462)	437,181	3
Total fixed maturities	<u>\$14,188,050</u>	<u>\$ 1,273,795</u>	<u>\$ (215,984)</u>	<u>\$ 15,245,861</u>	<u>100</u>

(1) Amount reported in the balance sheet.

(2) At fair value.

Securities, cash, and short-term investments held on deposit with various state and federal regulatory authorities had an amortized cost and fair value, respectively, of \$657 million and \$753 million at December 31, 2017 and \$600 million and \$663 million at December 31, 2016.

A schedule of fixed maturities available for sale by contractual maturity date at December 31, 2017 is shown below on an amortized cost basis and on a fair value basis. Actual maturity dates could differ from contractual maturities due to call or prepayment provisions.

	<u>Amortized Cost</u>	<u>Fair Value</u>
Fixed maturities available for sale:		
Due in one year or less	\$ 147,457	\$ 149,495
Due after one year through five years	682,932	720,186
Due after five years through ten years	1,397,473	1,567,972
Due after ten years through twenty years	4,701,591	5,519,917
Due after twenty years	7,861,000	8,789,769
Mortgage-backed and asset-backed securities	204,648	221,986
	<u>\$ 14,995,101</u>	<u>\$ 16,969,325</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

Analysis of investment operations:

	Year Ended December 31,		
	2017	2016	2015
Net investment income is summarized as follows:			
Fixed maturities available for sale	\$ 817,213	\$ 778,912	\$ 747,663
Policy loans	39,578	38,436	36,763
Other long-term investments	4,991	2,786	2,021
Short-term investments	948	447	95
	<u>862,730</u>	<u>820,581</u>	<u>786,542</u>
Less investment expense	(14,845)	(13,678)	(12,591)
Net investment income	<u>\$ 847,885</u>	<u>\$ 806,903</u>	<u>\$ 773,951</u>

An analysis of realized gains (losses) from investments is as follows:

Realized investment gains (losses):

Fixed maturities available for sale:

Sales and other	\$ 35,199	\$ (10,645)	\$ (9,479)
Other-than-temporary impairments	(245)	—	—
Other investments	(7,302)	(38)	688
Loss on redemption on debt	(4,041)	—	—
	<u>23,611</u>	<u>(10,683)</u>	<u>(8,791)</u>
Applicable tax	(6,021)	3,739	3,077
Realized gains (losses) from investments, net of tax	<u>\$ 17,590</u>	<u>\$ (6,944)</u>	<u>\$ (5,714)</u>

An analysis of the net change in unrealized investment gains (losses) is as follows:

Fixed maturities available for sale	\$ 916,413	\$ 551,658	\$ (1,163,295)
Other investments	5,008	2,143	(2,737)
Net change in unrealized gains (losses)	<u>\$ 921,421</u>	<u>\$ 553,801</u>	<u>\$ (1,166,032)</u>

Additional information about securities sold is as follows:

	At December 31,		
	2017	2016	2015
Fixed maturities available for sale:			
Proceeds from sales ⁽¹⁾	\$ 67,246	\$ 358,285	\$ 226,792
Gross realized gains	5,079	6,133	259
Gross realized losses	(1,100)	(32,608)	(16,894)

(1) Includes unsettled sales of \$17.9 million at December 31, 2016. There were no unsettled sales in 2017 or 2015.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

Fair value measurements: The following tables represent the fair value of fixed maturities measured on a recurring basis at December 31, 2017 and 2016:

Fair Value Measurements at December 31, 2017 Using:				
Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Fixed maturities available for sale:				
U.S. Government direct, guaranteed, and government-sponsored enterprises	\$ —	\$ 407,446	\$ —	\$ 407,446
States, municipalities, and political subdivisions..	44	1,219,671	—	1,219,715
Foreign governments	—	22,018	—	22,018
Corporates, by sector:				
Financial	—	3,673,089	62,006	3,735,095
Utilities	—	2,168,115	155,730	2,323,845
Energy	—	1,779,281	40,816	1,820,097
Other corporate sectors	—	6,468,541	324,258	6,792,799
Total corporates	—	14,089,026	582,810	14,671,836
Collateralized debt obligations	—	—	71,581	71,581
Other asset-backed securities	—	135,306	14,049	149,355
Redeemable preferred stocks, by sector:				
Financial	—	396,786	—	396,786
Utilities	—	30,588	—	30,588
Total redeemable preferred stocks	—	427,374	—	427,374
Total fixed maturities	\$ 44	\$ 16,300,841	\$ 668,440	\$ 16,969,325
Percentage of total	—%	96.1%	3.9%	100.0%

Fair Value Measurements at December 31, 2016 Using:				
Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Fixed maturities available for sale:				
U.S. Government direct, guaranteed, and government-sponsored enterprises	\$ —	\$ 372,798	\$ —	\$ 372,798
States, municipalities, and political subdivisions..	45,302	1,364,826	—	1,410,128
Foreign governments	—	23,077	—	23,077
Corporates, by sector:				
Financial	—	3,141,611	61,125	3,202,736
Utilities	—	1,959,143	153,900	2,113,043
Energy	—	1,598,976	27,115	1,626,091
Other corporate sectors	—	5,623,150	317,460	5,940,610
Total corporates	—	12,322,880	559,600	12,882,480
Collateralized debt obligations	—	—	63,503	63,503
Other asset-backed securities	—	56,694	—	56,694
Redeemable preferred stocks, by sector:				
Financial	—	408,027	—	408,027
Utilities	—	29,154	—	29,154
Total redeemable preferred stocks	—	437,181	—	437,181
Total fixed maturities	\$ 45,302	\$ 14,577,456	\$ 623,103	\$ 15,245,861
Percentage of total	0.3%	95.6%	4.1%	100.0%

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

The following table represents changes in fixed maturities measured at fair value on a recurring basis using significant unobservable inputs (Level 3).

	Analysis of Changes in Fair Value Measurements Using Significant Unobservable Inputs (Level 3)			
	Asset- backed securities	Collateralized debt Obligations	Corporates	Total
Balance at January 1, 2015	\$ —	\$ 63,232	\$ 512,714	\$ 575,946
Total gains or losses:				
Included in realized gains/losses	—	—	1,182	1,182
Included in other comprehensive income	—	11,365	(11,925)	(560)
Acquisitions	—	—	38,600	38,600
Sales	—	—	—	—
Amortization	—	5,536	17	5,553
Other ⁽¹⁾	—	(9,751)	(9,782)	(19,533)
Transfers into (out of) Level 3 ⁽²⁾	—	—	—	—
Balance at December 31, 2015	—	70,382	530,806	601,188
Total gains or losses:				
Included in realized gains/losses	—	—	788	788
Included in other comprehensive income	—	(3,943)	6,403	2,460
Acquisitions	—	—	33,662	33,662
Sales	—	—	—	—
Amortization	—	5,186	17	5,203
Other ⁽¹⁾	—	(8,122)	(12,076)	(20,198)
Transfers into (out of) Level 3 ⁽²⁾	—	—	—	—
Balance at December 31, 2016	—	63,503	559,600	623,103
Total gains or losses:				
Included in realized gains/losses	—	—	—	—
Included in other comprehensive income	410	9,654	10,900	20,964
Acquisitions	14,000	—	21,666	35,666
Sales	—	—	—	—
Amortization	—	4,914	17	4,931
Other ⁽¹⁾	(361)	(6,490)	(9,373)	(16,224)
Transfers into (out of) Level 3 ⁽²⁾	—	—	—	—
Balance at December 31, 2017	\$ 14,049	\$ 71,581	\$ 582,810	\$ 668,440

(1) Includes foreign exchange adjustments and principal repayments.

(2) There were no transfers in or out of Level 3 during the three years ended 2017.

Acquisitions of Level 3 investments in each of the years 2015 through 2017 are comprised of private-placement fixed maturities managed by an unaffiliated third-party.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

**Quantitative Information about Level 3
Fair Value Measurements
As of December 31, 2017**

	Fair Value	Valuation Techniques	Significant Unobservable Input	Range	Weighted Average
Asset-backed securities	\$ 14,049	Determination of credit spread	Credit rating	BBB	BBB
		Discounted cash flows	Discount rate	5.35%	5.35%
Collateralized debt obligations	71,581	Discounted cash flows	Discount rate	7.0 - 8.25%	8.03%
Private placement fixed maturities	\$ 582,810	Determination of credit spread	Credit rating	A+ to BB-	BBB
		Discounted cash flows	Discount rate	2.97 - 7.27%	3.93%
	<u>\$ 668,440</u>				

The private placement fixed maturities and asset-backed securities reported as Level 3 are managed by third party investment managers. These securities are valued based on the contractual cash flows discounted by a yield determined as a treasury benchmark adjusted for a credit spread. The credit spread is developed from observable indices for similar public fixed maturities and unobservable indices for private fixed maturities for corresponding credit ratings. However, the credit ratings for the securities are considered unobservable inputs, as they are assigned by the third party investment manager based on a quantitative and qualitative assessment of the credit underwritten. A higher (lower) credit rating would result in a higher (lower) valuation.

The collateral underlying collateralized debt obligations for which fair values are reported as Level 3 consists primarily of trust preferred securities issued by banks and insurance companies. Collateralized debt obligations are valued at the present value of expected future cash flows using an unobservable discount rate. Expected cash flows are determined by scheduling the projected repayment of the collateral assuming no future defaults, deferrals, or recoveries. The discount rate is risk-adjusted to take these items into account. A significant increase (decrease) in the discount rate will produce a significant decrease (increase) in fair value. Additionally, a significant increase (decrease) in the cash flow expectations would result in a significant increase (decrease) in fair value. For more information regarding valuation procedures, please refer to *Note 1—Significant Accounting Policies* under the caption *Fair Value Measurements, Investments in Securities*.

The following table presents transfers in and out of each of the valuation levels of fair values.

	2017			2016			2015		
	In	Out	Net	In	Out	Net	In	Out	Net
Level 1	\$ 42,372	\$ (597)	\$ 41,775	\$ 45,344	\$ —	\$ 45,344	\$ 17,252	\$ (49,744)	\$ (32,492)
Level 2	597	(42,372)	(41,775)	—	(45,344)	(45,344)	49,744	(17,252)	32,492
Level 3	—	—	—	—	—	—	—	—	—

Transfers into Level 2 from Level 3 result from the availability of observable market data when a security is valued at the end of a period. Transfers into Level 3 occur when there is a lack of observable market information. Transfers into Level 1 from Level 2 occur when direct quotes are available; transfers from Level 1 into Level 2 result when only observable market data and no direct quotes are available. Transfers between levels are recognized as of the end of the period of transfer.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

Other-than-temporary impairments (OTTI): Based on the Company's evaluation of its fixed maturities available for sale in an unrealized loss position in accordance with the OTTI policy as described in *Note 1—Significant Accounting Policies*, the Company concluded that there was an other-than-temporary impairment of \$245 thousand (\$159 thousand, net of tax) during the year ended December 31, 2017. For the two years ended December 31, 2016, there were no other-than-temporary impairments.

As of year end 2017, previously written down securities remaining in the portfolio were carried at a fair value of \$59 million, or less than 0.4% of the fair value of the fixed maturity portfolio. Torchmark is continuously monitoring the market conditions impacting its portfolio. While adverse market conditions for an extended duration could lead to some ratings downgrades in certain sectors, Torchmark has the ability and intent to hold these investments to recovery, and does not intend to sell or expect to be required to sell any of its securities in such a position.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

Unrealized gains/loss analysis: The following tables disclose gross unrealized investment losses by class and major sector of investments at December 31, 2017 and December 31, 2016 for the respective periods of time in a loss position. Torchmark considers these investments to be only temporarily impaired.

ANALYSIS OF GROSS UNREALIZED INVESTMENT LOSSES
At December 31, 2017

Description of Securities	Less than Twelve Months		Twelve Months or Longer		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Fixed maturities available for sale:						
Investment grade securities:						
U.S. Government direct, guaranteed, and government-sponsored enterprises	\$ 34,388	\$ (422)	\$ 47,514	\$ (951)	\$ 81,902	\$ (1,373)
States, municipalities and political subdivisions....	4,561	(21)	1,771	(9)	6,332	(30)
Foreign governments	—	—	—	—	—	—
Corporates, by sector:						
Financial	133,080	(652)	35,302	(1,429)	168,382	(2,081)
Utilities	48,562	(569)	32,345	(729)	80,907	(1,298)
Energy	23,463	(81)	67,775	(3,682)	91,238	(3,763)
Metals and mining	—	—	—	—	—	—
Other corporate sectors	220,661	(2,312)	163,886	(4,257)	384,547	(6,569)
Total corporates	425,766	(3,614)	299,308	(10,097)	725,074	(13,711)
Other asset-backed securities	—	—	—	—	—	—
Redeemable preferred stocks, by sector:						
Utilities	—	—	5,953	(97)	5,953	(97)
Total redeemable preferred stocks.....	—	—	5,953	(97)	5,953	(97)
Total investment grade securities	464,715	(4,057)	354,546	(11,154)	819,261	(15,211)
Below investment grade securities:						
States, municipalities and political subdivisions....	200	(105)	—	—	200	(105)
Corporates, by sector:						
Financial	—	—	84,432	(21,311)	84,432	(21,311)
Energy	8,114	(104)	75,204	(21,525)	83,318	(21,629)
Metals and mining	—	—	—	—	—	—
Other corporate sectors	25,334	(5,066)	54,383	(8,981)	79,717	(14,047)
Total corporates	33,448	(5,170)	214,019	(51,817)	247,467	(56,987)
Collateralized debt obligations	—	—	12,347	(7,653)	12,347	(7,653)
Redeemable preferred stocks, by sector:						
Financial	—	—	24,376	(2,727)	24,376	(2,727)
Total redeemable preferred stocks.....	—	—	24,376	(2,727)	24,376	(2,727)
Total below investment grade securities	33,648	(5,275)	250,742	(62,197)	284,390	(67,472)
Total fixed maturities	\$ 498,363	\$ (9,332)	\$ 605,288	\$ (73,351)	\$ 1,103,651	\$ (82,683)

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

ANALYSIS OF GROSS UNREALIZED INVESTMENT LOSSES
At December 31, 2016

Description of Securities	Less than Twelve Months		Twelve Months or Longer		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Fixed maturities available for sale:						
Investment grade securities:						
U.S. Government direct, guaranteed, and government-sponsored enterprises	\$ 321,133	\$ (8,553)	\$ 1,404	\$ (598)	\$ 322,537	\$ (9,151)
States, municipalities and political subdivisions....	32,178	(1,114)	683	(19)	32,861	(1,133)
Foreign governments	4,416	(62)	—	—	4,416	(62)
Corporates, by sector:						
Financial	479,669	(18,666)	64,335	(4,627)	544,004	(23,293)
Utilities	290,732	(11,000)	16,977	(1,604)	307,709	(12,604)
Energy	83,064	(1,076)	154,908	(18,127)	237,972	(19,203)
Metals and mining	5,936	(231)	5,789	(187)	11,725	(418)
Other corporate sectors	1,564,273	(65,131)	68,968	(6,495)	1,633,241	(71,626)
Total corporates	2,423,674	(96,104)	310,977	(31,040)	2,734,651	(127,144)
Other asset-backed securities	41,498	(337)	—	—	41,498	(337)
Redeemable preferred stocks, by sector:						
Utilities	5,857	(244)	—	—	5,857	(244)
Total redeemable preferred stocks	5,857	(244)	—	—	5,857	(244)
Total investment grade securities	2,828,756	(106,414)	313,064	(31,657)	3,141,820	(138,071)
Below investment grade securities:						
States, municipalities and political subdivisions....	—	—	357	(194)	357	(194)
Corporates, by sector:						
Financial	—	—	83,174	(22,592)	83,174	(22,592)
Energy	15,567	(385)	91,165	(24,736)	106,732	(25,121)
Metals and mining	32,478	(172)	34,463	(2,023)	66,941	(2,195)
Other corporate sectors	51,640	(291)	95,679	(10,017)	147,319	(10,308)
Total corporates	99,685	(848)	304,481	(59,368)	404,166	(60,216)
Collateralized debt obligations	—	—	9,714	(10,285)	9,714	(10,285)
Redeemable preferred stocks, by sector:						
Financial	—	—	19,912	(7,218)	19,912	(7,218)
Total redeemable preferred stocks	—	—	19,912	(7,218)	19,912	(7,218)
Total below investment grade securities	99,685	(848)	334,464	(77,065)	434,149	(77,913)
Total fixed maturities	\$ 2,928,441	\$ (107,262)	\$ 647,528	\$ (108,722)	\$ 3,575,969	\$ (215,984)

Gross unrealized losses decreased from \$216 million at year end 2016 to \$83 million at year end 2017, a decrease of \$133 million. The decrease in the gross unrealized losses from prior year was primarily attributable to the improved conditions during 2017 in the energy sector and broadly across all sectors.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

Additional information about fixed maturities available for sale in an unrealized loss position is as follows:

	Less than Twelve Months	Twelve Months or Longer	Total
Number of issues (CUSIP numbers) held:			
As of December 31, 2017	92	102	194
As of December 31, 2016	407	94	501

Torchmark's entire fixed maturity portfolio consisted of 1,502 issues at December 31, 2017 and 1,565 issues at December 31, 2016. The weighted-average quality rating of all unrealized loss positions at amortized cost was BBB- for 2017 and BBB+ for 2016.

Other investment information:

Other long-term investments consist of the following:

	Year Ended December 31,	
	2017	2016
Investment in limited partnerships	\$ 66,522	\$ 51,509
Commercial mortgage participations ⁽¹⁾	39,489	—
Other	2,548	2,343
Total	<u>\$ 108,559</u>	<u>\$ 53,852</u>

(1) A mortgage participation is a legal right to a prorata interest in a mortgage loan.

Torchmark did not have any invested assets that were non-income producing during the twelve months ended December 31, 2017.

Concentrations of Credit Risk: Torchmark maintains a diversified investment portfolio with limited concentration in any given issuer. At December 31, 2017, the investment portfolio, at fair value, consisted of the following:

Investment grade fixed maturities:

Corporate securities	82%
Securities of state and municipal governments	7
Government-sponsored enterprises	2
Other	1

Below investment grade fixed maturities:

Corporate securities	3
Other	1
Policy loans, which are secured by the underlying insurance policy values	3
Other investments	1
	<u>100%</u>

As of December 31, 2017, securities of state and municipal governments represented 7% of invested assets at fair value. Such investments are made throughout the U.S. At yearend 2017, the state and municipal bond portfolio at fair value was invested in securities issued within the following states: Texas (29%), Ohio (9%), Washington (8%), Illinois (7%), Michigan (5%), and Georgia (5%). Otherwise, there was no concentration within any given state greater than 5%.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 4—Investments (continued)

Corporate debt securities and redeemable preferred stocks represent 85% of Torchmark's investment portfolio. These investments are spread across a wide range of industries. Below are the ten largest industry concentrations held in the corporate portfolio of corporate debt securities and redeemable preferred stocks at December 31, 2017, based on fair value:

Insurance	16%
Electric utilities	12
Oil and natural gas pipelines	7
Banks	6
Transportation	4
Oil and natural gas exploration and production	4
Chemicals	4
Real estate investment trusts	4
Food	3
Metals and mining	3

At yearend 2017, 4% of invested assets at fair value were represented by fixed maturities rated below investment grade. Par value of these investments was \$790 million, amortized cost was \$702 million, and fair value was \$679 million. While these investments could be subject to additional credit risk, such risk should generally be reflected in their fair value.

Note 5—Deferred Acquisition Costs

An analysis of DAC is as follows:

	Year Ended December 31,		
	2017	2016	2015
Balance at beginning of year	\$ 3,783,158	\$ 3,617,135	\$ 3,457,397
Additions:			
Deferred during period:			
Commissions	465,920	436,252	401,166
Other expenses	194,214	199,066	211,015
Total deferred	660,134	635,318	612,181
Foreign exchange adjustment	5,712	2,180	—
Adjustment attributable to unrealized investment losses ⁽¹⁾	—	—	8,682
Total additions	665,846	637,498	620,863
Deductions:			
Amortized during period	(490,403)	(469,063)	(445,625)
Foreign exchange adjustment	—	—	(15,500)
Adjustment attributable to unrealized investment gains ⁽¹⁾	(538)	(2,412)	—
Total deductions	(490,941)	(471,475)	(461,125)
Balance at end of year	<u>\$ 3,958,063</u>	<u>\$ 3,783,158</u>	<u>\$ 3,617,135</u>

(1) Represents amounts pertaining to investments relating to universal life-type products.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 6—Discontinued Operations

At December 31, 2015, Torchmark met the criteria to account for its Medicare Part D Prescription Drug Plan business as a discontinued operation. Historically, the business was a reportable segment. Effective July 1, 2016, Torchmark sold its Medicare Part D Prescription Drug Plan business to an unaffiliated third party.

The sale resulted in a net gain of \$1.8 million (\$1.2 million net of tax) in 2016. The operating results from discontinued operations are reflected in income for the twelve months ended December 31, 2017. The remaining assets and liabilities reflected on the Torchmark balance sheet related to discontinued operations are receivables and payables associated with the 2016 and prior plan years that are expected to be settled in the ordinary course of business during 2018.

The net assets related to discontinued operations at December 31, 2017 and 2016 were as follows:

	At December 31,	
	2017	2016
Assets:		
Due premiums	\$ 3,945	\$ 8,840
Other receivables ⁽¹⁾	64,575	118,692
Total assets related to discontinued operations	68,520	127,532
Liabilities:		
Risk sharing payable	8,731	8,374
Current and deferred income taxes payable	1,077	3,820
Other ⁽²⁾	40,046	15,230
Total liabilities related to discontinued operations	49,854	27,424
Net assets	\$ 18,666	\$ 100,108

(1) At December 31, 2017, other receivables included \$65 million from Centers for Medicare and Medicaid Services (CMS). At December 31, 2016, the comparable amounts were \$50 million from CMS and \$69 million from drug manufacturer rebates.

(2) At December 31, 2017, the balance included \$37.3 million due to CMS. At December 31, 2016, the balance includes \$3.6 million contingent sale price reserve.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 6—Discontinued Operations (continued)

Income from discontinued operations for the three years ended December 31, 2017 is as follows:

	Year Ended December 31,		
	2017	2016	2015
Revenue:			
Health premium	\$ —	\$ 222,840	\$ 260,657
Benefits and expenses:			
Health policyholder benefits	3,827	183,423	213,114
Amortization of deferred acquisition costs	—	3,747	3,506
Commissions, premium taxes, and non-deferred acquisition expenses	763	16,396	20,909
Other operating expense	1,209	5,377	6,502
Total benefits and expenses	<u>5,799</u>	<u>208,943</u>	<u>244,031</u>
Income before income taxes for discontinued operations	(5,799)	13,897	16,626
Gain from sale of discontinued operations	—	1,779	—
Income taxes	2,030	(5,487)	(5,819)
Income from discontinued operations	<u>\$ (3,769)</u>	<u>\$ 10,189</u>	<u>\$ 10,807</u>

Income taxes paid related to discontinued operations for the three years ended December 31, 2017 were as follows:

	Year Ended December 31,		
	2017	2016	2015
Income taxes paid	\$ 714	\$ 15,271	\$ 3,409

Note 7—Liability for Unpaid Claims

Activity in the liability for unpaid health claims is summarized as follows:

	Year Ended December 31,		
	2017	2016	2015
Balance at beginning of year	\$ 143,128	\$ 137,120	\$ 128,265
Incurred related to:			
Current year	520,528	510,075	502,009
Prior years	(8,048)	(1,127)	(7,845)
Total incurred	<u>512,480</u>	<u>508,948</u>	<u>494,164</u>
Paid related to:			
Current year	394,506	386,278	379,037
Prior years	114,237	116,662	106,272
Total paid	<u>508,743</u>	<u>502,940</u>	<u>485,309</u>
Balance at end of year	<u>\$ 146,865</u>	<u>\$ 143,128</u>	<u>\$ 137,120</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 7—Liability for Unpaid Claims (continued)

At the end of each period, the liability for unpaid health claims includes an estimate of claims incurred but not yet reported to the Company. Such estimates are updated regularly based upon the Company's most recent claims data with recognition of emerging experience trends. Because of the nature of the Company's health business, the payment lags are relatively short and most claims are fully paid within a year from the time incurred. Fluctuations in claims experience can lead to either over or under estimation of the liability for any given year. The difference between the estimate made at the end of the prior period and the actual experience during the period is reflected above under the caption "Incurred related to: Prior years."

The liability for unpaid health claims is included within "Policy claims and other benefits payable" in the *Consolidated Balance Sheets*.

Short-Duration Contracts

Although Torchmark primarily sells long-duration contracts for both life and health, the Company also has a limited amount of group health products that qualify as short-duration contracts in accordance with the applicable guidance.

The following table illustrates the total incurred claims for short-duration products over the last five years for the year ended December 31, 2017. Claim frequency is determined by duration and incurred date.

Accident Year	For the years ended December 31, 2017					As of December 31, 2017	
	Cumulative incurred claims ⁽¹⁾					Total of incurred-but-not-reported liabilities plus expected development on reported claims	Cumulative number of reported claims ⁽¹⁾ (In thousands)
	2013	2014	2015	2016	2017		
2013	\$ 84,111	\$ 82,644	\$ 83,151	\$ 83,119	\$ 83,103	\$ —	1,337
2014		101,407	99,876	99,810	99,777	—	1,600
2015			141,667	141,460	141,259	17	2,224
2016				140,944	138,899	431	2,158
2017					134,677	24,259	1,765
				Total	\$ 597,715	\$ 24,707	

(1) The incurred claims and cumulative number of reported claims for all years prior to 2017 are unaudited.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 7—Liability for Unpaid Claims (continued)

This table illustrates the total cumulative paid claims and allocated claims for short-duration products over the last five years for the year ended December 31, 2017.

Accident Year	Cumulative paid claims ⁽¹⁾				
	For the years ended December 31,				
	2013	2014	2015	2016	2017
2013	\$ 68,159	\$ 82,408	\$ 83,131	\$ 83,119	\$ 83,103
2014		81,054	99,545	99,791	99,777
2015			115,922	140,982	141,242
2016				114,720	138,468
2017					110,418
				Total	573,008
					Short-duration claim liability as of December 31, 2017
					24,707
					Total incurred claims & IBNR
					<u>\$597,715</u>

(1) The cumulative paid claims for all years prior to 2017 are unaudited.

Below is the reconciliation of the net incurred and paid claims development tables to the liability for "Policy claims and other benefits payable" in the *Consolidated Balance Sheets*.

	December 31, 2017	December 31, 2016
Policy claims and other benefits payable:		
Short-duration products	\$ 24,707	\$ 26,721
Insurance lines other than short duration—health	122,158	116,407
Total health	146,865	143,128
Insurance lines other than short duration—life	186,429	156,437
Total policy claims and other benefits payable	<u>\$ 333,294</u>	<u>\$ 299,565</u>

Note 8—Income Taxes

The components of income taxes were as follows:

	Year Ended December 31,		
	2017	2016	2015
Income tax expense (benefit) from continuing operations	\$ (627,615)	\$ 232,645	\$ 249,894
Shareholders' equity:			
Other comprehensive income (loss)	318,475	186,206	(411,646)
Tax basis compensation expense (from the exercise of stock options and vesting of restricted stock awards) in excess of amounts recognized for financial reporting purposes	—	—	(17,577)
	<u>\$ (309,140)</u>	<u>\$ 418,851</u>	<u>\$ (179,329)</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 8—Income Taxes (continued)

Income tax (benefit) expense from continuing operations consists of:

	Year Ended December 31,		
	2017	2016	2015
Current income tax (benefit) expense	\$ 138,262	\$ 132,806	\$ 174,284
Deferred income tax (benefit) expense	(765,877)	99,839	75,610
	\$ (627,615)	\$ 232,645	\$ 249,894

In each of the years 2015 through 2017, deferred income tax (benefit) expense was incurred because of certain differences between net income before income taxes as reported on the *Consolidated Statements of Operations* and taxable income as reported on Torchmark's income tax returns. As explained in *Note 1—Significant Accounting Policies*, these differences caused the financial statement book values of some assets and liabilities to be different from their respective tax bases.

As discussed in *Note 1—Significant Accounting Policies*, due to the passage of the Tax Legislation before December 31, 2017, the Company recorded \$877 million reduction in deferred income tax expense related to a one-time adjustment to reduce its net deferred tax liability as of December 22, 2017, as required by ASC 740 *Income Taxes*, due to the reduction in the income tax rate. This adjustment to the Company's net deferred tax liability included \$252 million related to items included in AOCI.

Although many aspects of the Tax Legislation are not effective until 2018, the Company recorded a reasonable estimate for the tax reform adjustment in accordance with SAB 118. We will continue to analyze relevant information to complete our accounting for income taxes which may result in an adjustment to our estimate in 2018. The accounting is expected to be complete when the 2017 U.S. corporate income tax return is filed later in 2018.

The effective income tax rate differed from the expected 35% rate as shown below:

	Year Ended December 31,					
	2017	%	2016	%	2015	%
Expected income taxes	\$ 290,727	35.0	\$ 270,282	35.0	\$ 268,165	35.0
Increase (reduction) in income taxes resulting from:						
Tax reform adjustment	(877,400)	(105.6)	—	—	—	—
Low income housing investments	(18,515)	(2.2)	(18,202)	(2.4)	(19,031)	(2.5)
Share-based awards	(19,549)	(2.4)	(18,653)	(2.4)	—	—
Other	(2,878)	(0.4)	(782)	(0.1)	760	0.1
Income tax expense (benefit) from continuing operations	\$ (627,615)	(75.6)	\$ 232,645	30.1	\$ 249,894	32.6

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 8—Income Taxes (continued)

The tax effects of temporary differences that gave rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	December 31,	
	2017	2016
Deferred tax assets:		
Fixed maturity investments	\$ 8,692	\$ 15,004
Carryover of tax losses	4,760	3,906
Total gross deferred tax assets	13,452	18,910
Deferred tax liabilities:		
Unrealized gains	380,251	315,509
Employee and agent compensation	65,576	92,131
Deferred acquisition costs	618,889	975,873
Future policy benefits, unearned and advance premiums, and policy claims	248,752	391,451
Other liabilities	11,289	3,987
Total gross deferred tax liabilities	1,324,757	1,778,951
Net deferred tax liability	\$ 1,311,305	\$ 1,760,041

Income Tax Return: Torchmark and its subsidiaries, excluding Family Heritage Life Insurance Company (Family Heritage), file a life-nonlife consolidated federal income tax return. Family Heritage files its federal income tax return on a separate company basis. The statutes of limitations for the Internal Revenue Service's examination and assessment of additional tax are closed for all tax years prior to 2014 with respect to Torchmark's consolidated and Family Heritage's federal income tax returns. Management believes that adequate provision has been made in the consolidated financial statements for any potential assessments that may result from current or future tax examinations and other tax-related matters for all open years.

Valuations: Torchmark has net operating loss carryforwards of approximately \$22.7 million at December 31, 2017 which will begin to expire in 2033 if not otherwise used to offset future taxable income. A valuation allowance is to be provided when it is more likely than not that deferred tax assets will not be realized by the Company. No valuation allowance has been recorded relating to Torchmark's deferred tax assets as management believes Torchmark will more likely than not have sufficient taxable income in future periods to fully realize its existing deferred tax assets.

Torchmark's tax liability is adjusted to include a provision for uncertain tax positions taken or expected to be taken in a tax return. However, during the years 2015 through 2017, Torchmark did not have any uncertain tax positions which resulted in unrecognized tax benefits.

Tax penalties: Torchmark's continuing practice is to recognize interest and penalties related to income tax matters in income tax expense. The Company recognized interest income of \$5 thousand, \$9 thousand, and \$11 thousand, net of federal income tax expense, in its *Consolidated Statements of Operations* for 2017, 2016, and 2015, respectively. The Company had no accrued interest or penalties at December 31, 2017 or 2016.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits

Torchmark has qualified noncontributory defined benefit pension plans and contributory savings plans which cover substantially all employees. There are also two nonqualified noncontributory supplemental executive retirement plans (SERPs) which cover a limited number of employees. The total cost of these retirement plans charged to operations was as follows:

Year Ended December 31,	Defined Contribution Plans ⁽¹⁾	Defined Benefit Pension Plans ⁽²⁾
2017	\$ 4,145	\$ 28,828
2016	3,614	24,202
2015	3,429	29,230

(1) 401K plans

(2) Qualified pension plans and SERPs

Torchmark accrues expense for the defined contribution plans based on a percentage of the employees' contributions. The plans are funded by the employee contributions and a Torchmark contribution equal to the amount of accrued expense. Plan contributions are both mandatory and discretionary, depending on the terms of the plan.

Pension Plans: Cost for the defined benefit pension plans has been calculated on the projected unit credit actuarial cost method. All plan measurements for the defined benefit plans are as of December 31st of the respective year. The defined benefit pension plans covering the majority of employees are qualified and funded. Contributions are made to funded pension plans subject to minimums required by regulation and maximums allowed for tax purposes. Defined benefit plan contributions were \$21.3 million in 2017, \$15.8 million in 2016, and \$15.5 million in 2015. Torchmark estimates as of December 31, 2017 that it will contribute an amount in the range of \$30 million to \$40 million to these plans in 2018. The actual amount of contribution may be different from this estimate.

Torchmark has two SERPs, one of which is active and provides to a limited number of executives an additional supplemental defined pension benefit. The supplemental benefit is based on the participant's qualified plan benefit without consideration to the regulatory limits on compensation and benefit payments applicable to qualified plans, except that eligible compensation is capped at \$1 million. This SERP is nonqualified and unfunded. However, a Rabbi Trust has been established to support the liability for this plan. This trust consists of life insurance policies on the lives of plan participants with an unaffiliated insurance carrier as well as an investment account.

Since this plan is nonqualified, the investments and the policyholder value of the insurance policies in the Rabbi Trust are not included as defined benefit plan assets, but rather assets of the Company. They are included in "Other Assets" in the *Consolidated Balance Sheets*.

The second supplemental benefit pension plan is limited to a very select group of employees and was closed as of December 31, 1994. It provides the full benefits that an employee would have otherwise received from a defined benefit plan in the absence of the limitation on benefits payable under a qualified plan. This plan is also nonqualified and unfunded. Pension cost for both supplemental defined benefit plans is determined in the same manner as for the qualified defined benefit plans.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

The following table includes activity for the SERPs for the three years ended December 31, 2017.

	Year Ended December 31,		
	2017	2016	2015
Premiums paid for insurance coverage	\$ 2,050	\$ 2,050	\$ 10,068
	December 31,		
	2017	2016	
Total investments:			
Company owned life insurance	\$ 40,273	\$ 37,267	
Exchange traded funds	55,442	48,999	
	\$ 95,715	\$ 86,266	
Liability:			
Active plan	\$ 81,457	\$ 74,687	
Closed plan	3,008	3,220	

Plan assets in the funded plans consist primarily of investments in marketable fixed maturities and equity securities and are valued at fair value. Torchmark measures the fair value of its financial assets, including the assets in its benefit plans, in accordance with accounting guidance which establishes a hierarchy for asset values and provides a methodology for the measurement of value. Please refer to *Note 1—Significant Accounting Policies* under the caption *Fair Value Measurements, Investments in Securities* for a complete discussion of valuation procedures. The following table presents the assets of Torchmark's defined benefit pension plans for the years ended December 31, 2017 and 2016.

Pension Assets by Component at December 31, 2017

	Fair Value Determined by:				Total Amount	% to Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)			
Corporate bonds:						
Financial	\$	\$ 43,451	\$	\$ 43,451	12	
Utilities		46,144		46,144	12	
Energy		25,023		25,023	7	
Other corporates		65,888		65,888	17	
Total corporate bonds	—	180,506	—	180,506	48	
Exchange traded fund ⁽¹⁾	164,351			164,351	43	
Other bonds		256		256	—	
Other long-term investments		2,304		2,304	1	
Guaranteed annuity contract ⁽²⁾		21,202		21,202	6	
Short-term investments	3,984			3,984	1	
Other	5,021			5,021	1	
Grand Total	\$ 173,356	\$ 204,268	\$ —	\$ 377,624	100	

(1) A fund including marketable securities that mirror the S&P 500 index.

(2) Representing a guaranteed annuity contract issued by Torchmark's subsidiary, American Income Life Insurance Company, to fund the obligations of the American Income Pension Plan.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

Pension Assets by Component at December 31, 2016

	Fair Value Determined by:				Total Amount	% to Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)			
Corporate bonds:						
Financial	\$	\$	41,578	\$	41,578	13
Utilities			43,890		43,890	13
Energy			25,427		25,427	8
Other corporates			49,141		49,141	15
Total corporate bonds	—	160,036	—	160,036	49	
Exchange traded fund ⁽¹⁾	134,771			134,771	41	
Other bonds		258		258	—	
Guaranteed annuity contract ⁽²⁾		18,997		18,997	6	
Short-term investments	7,391			7,391	2	
Other	7,418			7,418	2	
Grand Total	<u>\$ 149,580</u>	<u>\$ 179,291</u>	<u>\$ —</u>	<u>\$ 328,871</u>	<u>100</u>	

(1) A fund including marketable securities that mirror the S&P 500 index.

(2) Representing a guaranteed annuity contract issued by Torchmark's subsidiary, American Income Life Insurance Company, to fund the obligations of the American Income Pension Plan.

Torchmark's investment objectives for its plan assets include preservation of capital, preservation of purchasing power, and long-term growth. Torchmark seeks to preserve capital through investments made in high quality securities with adequate diversification by issuer and industry sector to minimize risk. The portfolio is monitored continuously for changes in quality and diversification mix. The preservation of purchasing power is intended to be accomplished through asset growth, exclusive of contributions and withdrawals, in excess of the rate of inflation. Torchmark intends to maintain investments that when combined with future plan contributions will produce adequate long-term growth to provide for all plan obligations. It is also Torchmark's objective that the portfolio's investment return will meet or exceed the return of a balanced market index.

The majority of the securities in the portfolio are highly marketable so that there will be adequate liquidity to meet projected payments. There are no specific policies calling for asset durations to match those of benefit obligations.

Allowed investments are limited to equities, fixed maturities, and short-term investments (invested cash). The assets are to be invested in a mix of equity and fixed income investments that best serve the objectives of the pension plan. Factors to be considered in determining the asset mix include funded status, annual pension expense, annual pension contributions, and balance sheet liability. Equities can include common and preferred stocks, securities convertible into equities, mutual funds and exchange traded funds that invest in equities, equity interests in limited partnerships, and other equity-related investments. Primarily, equities are listed on major exchanges and adequate market liquidity is required. Fixed maturities primarily consist of marketable debt securities rated investment grade at purchase by a major rating agency. Short-term investments include fixed maturities with maturities less than one year and invested cash. Short-term investments in commercial paper must be rated at least A-2 by Standard & Poor's with the issuer rated investment grade. Invested cash is limited to banks rated A or higher. Investments outside of the aforementioned list are not permitted, except by prior approval of the Plan's Trustees.

The investment portfolio is to be well diversified to avoid undue exposure to a single sector, industry, business, or security. The equity and fixed maturity portfolios are not permitted to invest in any single issuer that would exceed 10% of total plan assets at the time of purchase. Torchmark does not employ any other special risk management techniques, such as derivatives, in managing the pension investment portfolio.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

Torchmark's equity securities include an exchange traded fund that mirrors the S&P 500 index which better aligns with a passive approach rather than an actively managed portfolio. At December 31, 2017, there were no restricted investments contained in the portfolio. Plan contributions have been invested primarily in fixed maturity and equity securities during the three years ended December 31, 2017.

The following table discloses the assumptions used to determine Torchmark's pension liabilities and costs for the appropriate periods. The discount and compensation increase rates are used to determine current year projected benefit obligations and subsequent year pension expense. The long-term rate of return is used to determine current year expense. Differences between assumptions and actual experience are included in actuarial gain or loss.

Weighted Average Pension Plan Assumptions

For Benefit Obligations at December 31:	2017	2016	
Discount Rate	3.75%	4.27%	
Rate of Compensation Increase	4.37	4.31	
For Periodic Benefit Cost for the Year:	2017	2016	2015
Discount Rate	4.27%	4.64%	4.23%
Expected Long-Term Returns	6.96	7.19	6.96
Rate of Compensation Increase	4.31	4.33	4.35

The discount rate is determined based on the expected duration of plan liabilities. A yield is then derived based on the current market yield of a hypothetical portfolio of higher-quality corporate bonds which match the liability duration. The rate of compensation increase is projected based on Company experience, modified as appropriate for future expectations. The expected long-term rate of return on plan assets is management's best estimate of the average rate of earnings expected to be received on the assets invested in the plan over the benefit period. In determining this assumption, consideration is given to the historical rate of return earned on the assets, the projected returns over future periods, and the discount rate used to compute benefit obligations.

Net periodic pension cost for the defined benefit plans by expense component was as follows:

	Year Ended December 31,		
	2017	2016	2015
Service cost—benefits earned during the period	\$ 17,942	\$ 15,502	\$ 15,902
Interest cost on projected benefit obligation	22,124	21,631	19,887
Expected return on assets	(23,597)	(23,127)	(21,204)
Net amortization	12,281	10,135	14,465
Recognition of actuarial loss	78	61	180
Net periodic pension cost	\$ 28,828	\$ 24,202	\$ 29,230

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

An analysis of the impact on other comprehensive income (loss) concerning pensions and other postretirement benefits is as follows:

	Year Ended December 31,		
	2017	2016	2015
Balance at January 1	\$ (173,883)	\$ (152,149)	\$ (152,999)
Amortization of:			
Prior service cost	476	477	377
Net actuarial (gain) loss ⁽¹⁾	11,960	9,691	14,209
Total amortization	12,436	10,168	14,586
Plan amendments	—	—	(2,104)
Experience gain (loss)	(31,933)	(31,902)	(11,632)
Balance at December 31	<u>\$ (193,380)</u>	<u>\$ (173,883)</u>	<u>\$ (152,149)</u>

(1) Includes amortization of postretirement benefits other than pensions of \$155 thousand in 2017, \$33 thousand in 2016, and \$120 thousand in 2015.

The following table presents a reconciliation from the beginning to the end of the year of the projected benefit obligation and plan assets for pensions. This table also presents the amounts previously recognized as a component of accumulated other comprehensive income.

Pension Benefits

	Year Ended December 31,	
	2017	2016
Changes in benefit obligation:		
Obligation at beginning of year	\$ 527,522	\$ 476,581
Service cost	17,942	15,502
Interest cost	22,124	21,631
Plan amendments	—	—
Actuarial loss (gain)	55,369	34,667
Benefits paid	(20,351)	(20,859)
Obligation at end of year	<u>602,606</u>	<u>527,522</u>
Changes in plan assets:		
Fair value at beginning of year	328,871	307,596
Return on assets	47,832	26,377
Contributions	21,272	15,757
Benefits paid	(20,351)	(20,859)
Fair value at end of year	<u>377,624</u>	<u>328,871</u>
Funded status at year end	<u>\$ (224,982)</u>	<u>\$ (198,651)</u>
Amounts recognized in accumulated other comprehensive income consist of:		
Net loss (gain)	\$ 186,563	\$ 167,313
Prior service cost	4,135	4,611
Net amounts recognized at year end	<u>\$ 190,698</u>	<u>\$ 171,924</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

The portion of other comprehensive income that is expected to be reflected in pension expense in 2018 is as follows:

Amortization of prior service cost	\$ 476
Amortization of net actuarial loss	14,543
Total	<u>\$ 15,019</u>

The accumulated benefit obligation (ABO) for Torchmark’s funded defined benefit pension plans was \$466 million and \$411 million at December 31, 2017 and 2016, respectively. In the nonqualified plans, the ABO was \$75 million at December 31, 2017 and \$69 million at 2016.

Torchmark has estimated its expected pension benefits to be paid over the next ten years as of December 31, 2017. These estimates use the same assumptions that measure the benefit obligation at December 31, 2016, taking estimated future employee service into account. Those estimated benefits are as follows:

For the year(s)

2018	\$ 20,375
2019	22,143
2020	23,840
2021	25,239
2022	27,090
2023-2027	160,075

Postretirement Benefit Plans Other Than Pensions: Torchmark provides a small postretirement life insurance benefit for most retired employees, and also provides additional postretirement life insurance benefits for certain key employees. The majority of the life insurance benefits are accrued over the working lives of active employees. Otherwise, Torchmark does not provide postretirement benefits other than pensions and the life insurance benefits described above.

Torchmark’s postretirement defined benefit plans other than pensions are not funded. Liabilities for these plans are measured as of December 31 for the appropriate year.

The components of net periodic postretirement benefit cost for plans other than pensions are as follows:

	Year Ended December 31,		
	2017	2016	2015
Service cost	\$ —	\$ —	\$ —
Interest cost on benefit obligation	1,132	1,139	1,075
Expected return on plan assets	—	—	—
Net amortization	155	33	120
Recognition of net actuarial (gain) loss	167	(132)	367
Net periodic postretirement benefit cost	<u>\$ 1,454</u>	<u>\$ 1,040</u>	<u>\$ 1,562</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

The following table presents a reconciliation of the benefit obligation and plan assets from the beginning to the end of the year. As these plans are unfunded, funded status is equivalent to the accrued benefit liability.

Benefits Other Than Pensions

	Year Ended December 31,	
	2017	2016
Changes in benefit obligation:		
Obligation at beginning of year	\$ 23,721	\$ 22,479
Service cost	—	—
Interest cost	1,132	1,139
Actuarial loss (gain)	1,045	412
Benefits paid	(285)	(309)
Obligation at end of year	<u>25,613</u>	<u>23,721</u>
Changes in plan assets:		
Fair value at beginning of year	—	—
Return on assets	—	—
Contributions	285	309
Benefits paid	(285)	(309)
Fair value at end of year	<u>—</u>	<u>—</u>
Funded status at year end	<u>\$ (25,613)</u>	<u>\$ (23,721)</u>
Amounts recognized in accumulated other comprehensive income:		
Net loss ⁽¹⁾	\$ 2,682	\$ 1,959
Net amounts recognized at year end	<u>\$ 2,682</u>	<u>\$ 1,959</u>

(1) The net loss for benefit plans other than pensions reduces other comprehensive income.

The table below presents the assumptions used to determine the liabilities and costs of Torchmark's postretirement benefit plans other than pensions.

**Weighted Average Assumptions for Postretirement
Benefit Plans Other Than Pensions**

For Benefit Obligations at December 31:			
	2017	2016	
Discount Rate	3.76%	4.29%	
For Periodic Benefit Cost for the Year:			
	2017	2016	2015
Discount Rate	4.29%	4.66%	4.23%

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 9—Postretirement Benefits (continued)

Estimated Future Payments for Post-Retirement Benefit Plans Other Than Pensions

For the year(s)

2018	\$	1,228
2019		1,278
2020		1,311
2021		1,344
2022		1,386
2023-2027		7,515

Note 10—Supplemental Disclosures of Cash Flow Information

The following table summarizes Torchmark's noncash transactions, which are not reflected on the *Consolidated Statements of Cash Flows*:

	Year Ended December 31,		
	2017	2016	2015
Stock-based compensation not involving cash	\$ 37,034	\$ 26,326	\$ 28,664
Commitments for low-income housing interests	33,846	56,818	68,949
Exchanges of fixed maturity investments	84,312	224,901	—
Net unsettled security trades	—	15,020	—

The following table summarizes certain amounts paid during the period:

	Year Ended December 31,		
	2017	2016	2015
Interest paid	\$ 82,494	\$ 81,338	\$ 74,792
Income taxes paid	74,379	79,790	110,650

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 11—Debt

The following table presents information about the terms and outstanding balances of Torchmark's debt.

Selected Information about Debt Issues

	Annual Interest Rate	Issue Date	Periodic Interest Payments Due	As of December 31,			
				2017		2016	
				Outstanding Principal (Par Value)	Outstanding Principal (Book Value)	Outstanding Principal (Fair Value)	Outstanding Principal (Book Value)
Long-term debt:							
Notes, due 5/15/23 ^(3,5)	7.875%	5/93	5/15 & 11/15	\$ 165,612	\$ 164,284	\$ 195,786	\$ 164,095
Senior Notes, due 6/15/19 ^(3,7) ...	9.250%	6/09	6/15 & 12/15	292,647	291,888	320,697	291,424
Senior Notes, due 9/15/22 ^(3,7) ...	3.800%	9/12	3/15 & 9/15	150,000	148,477	155,000	148,189
Junior Subordinated Debentures due 12/15/52 ^(4,8,12) ..	5.875%	9/12	quarterly	—	—	—	120,929
Junior Subordinated Debentures due 3/15/36 ^(4,6,12) ...	4.888% ⁽¹³⁾	(11)	quarterly	20,000	20,000	20,000	20,000
Junior Subordinated Debentures due 6/15/56 ^(4,9)	6.125%	4/16	quarterly	300,000	290,460	321,120	290,403
Junior Subordinated Debentures due 11/17/57 ^(4,10) ...	5.275%	11/17	6/15 & 12/15	125,000	123,342	122,039	—
Term loan due 5/17/21 ^(1,6)	2.600% ⁽¹⁴⁾	6/16	monthly	98,125	98,125	98,125	100,000
				<u>1,151,384</u>	<u>1,136,576</u>	<u>1,232,767</u>	<u>1,135,040</u>
Less current maturity of term loan				4,375	4,375	4,375	1,875
Total long-term debt				<u>1,147,009</u>	<u>1,132,201</u>	<u>1,228,392</u>	<u>1,133,165</u>
Short-term debt:							
Current maturity of term loan				4,375	4,375	4,375	1,875
Commercial paper ⁽²⁾				324,250	323,692	323,692	262,600
Total short-term debt				<u>328,625</u>	<u>328,067</u>	<u>328,067</u>	<u>264,475</u>
Total debt				<u>\$ 1,475,634</u>	<u>\$ 1,460,268</u>	<u>\$ 1,556,459</u>	<u>\$ 1,397,640</u>

- (1) The term loan has higher priority than all other debt issues.
- (2) Commercial paper has priority over all other debt except the term loan.
- (3) All securities, other than the term loan, commercial paper and Junior Subordinated Debentures have equal priority with one another.
- (4) All Junior Subordinated Debentures have equal priority, but are subordinate to all other issues.
- (5) Not callable.
- (6) Callable anytime.
- (7) Callable subject to "make-whole" premium.
- (8) Redeemed on December 22, 2017.
- (9) Callable at any time on or after June 15, 2021, and prior to this date upon the occurrence of a Tax Event or Rating Agency Event.
- (10) Callable at any time on or after November 17, 2022, and prior to this date upon the occurrence of a Tax Event or Rating Agency Event.
- (11) Assumed upon November 1, 2012 acquisition of Family Heritage.
- (12) Quarterly payments on the 15th of March, June, September, and December.
- (13) Interest paid at 3 Month LIBOR plus 330 basis points, resets each quarter.
- (14) Interest paid at 1 Month LIBOR plus 125 basis points, resets each month.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 11—Debt (continued)

Contractual Debt Obligations: The following table presents expected scheduled principal payments under our contractual debt obligations:

	Year Ended December 31,					Thereafter
	2018	2019	2020	2021	2022	
Debt obligations	\$ 328,625	\$ 299,522	\$ 9,375	\$ 77,500	\$ 150,000	\$ 610,612

Funded debt: On November 17, 2017, Torchmark completed the issuance and sale of \$125 million in aggregate principal of Torchmark's 5.275% Junior Subordinated Debentures due 2057. The debentures were sold in a private placement pursuant to exemptions from the registration requirements of the Securities Act of 1933. The initial purchaser of the debentures was outside the United States. The net proceeds from the sale of the debentures were \$123.3 million, after giving effect to the discount payable to the initial purchaser and expenses of the offering of the debentures. Torchmark used the net proceeds from the offering of the debentures to repay the \$125 million outstanding principal, plus accrued interest of \$143 thousand on the 5.875% Junior Subordinated Debentures on December 22, 2017. The Debentures were due December 15, 2052 and were callable beginning December 15, 2017.

On April 5, 2016, Torchmark completed the issuance and sale of \$300 million in aggregate principal of Torchmark's 6.125% Junior Subordinated Debentures due 2056. The debentures were sold pursuant to Torchmark's shelf registration statement on Form S-3, filed September 25, 2015. The net proceeds from the sale of the debentures were \$290 million, after giving effect to the underwriting discount and expenses of the offering of the debentures. Torchmark used the net proceeds from the offering of the debentures to repay the \$250 million outstanding principal, plus accrued interest of \$8 million, on the 6.375% Senior Notes that were due June 15, 2016. The remaining proceeds were used for general corporate purposes.

Credit Facility: On May 17, 2016, Torchmark amended its credit facility to include, as a part of the facility, the issuance of a \$100 million term loan and to extend the maturity date of the entire credit facility to May 2021. The facility is further designated as a back-up credit line for a commercial paper program under which the Company may either borrow from the credit line or issue commercial paper at any time, with total commercial paper outstanding not to exceed the facility maximum of \$750 million, less any letters of credit issued. Interest is charged at variable rates. The term loan will be repaid on a redemption schedule which provides for quarterly installments that began June 30, 2017 that escalate each annual period with a balloon payment of \$75 million due in May 2021. Interest on the term loan is computed and paid monthly at 125 basis points plus 1 Month LIBOR. In accordance with the agreement, Torchmark is subject to certain covenants regarding capitalization. As of December 31, 2017, the Company was in full compliance with these covenants.

Commercial paper outstanding and any amortization payments of the term loan due within one year are reported as short-term debt on the *Consolidated Balance Sheets*. A table presenting selected information concerning Torchmark's commercial paper borrowings is presented below.

Credit Facility - Commercial Paper

	At December 31,	
	2017	2016
Balance at end of period (at par value)	\$ 324,250	\$ 262,850
Annualized interest rate	1.78%	0.96%
Letters of credit outstanding	\$ 177,000	\$ 177,000
Remaining amount available under credit line	248,750	310,150

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 11—Debt (continued)

	Year Ended December 31,		
	2017	2016	2015
Average balance outstanding during period	\$ 323,429	\$ 301,550	\$ 350,851
Daily-weighted average interest rate (annualized)	1.30%	0.83%	0.43%
Maximum daily amount outstanding during period	\$ 455,912	\$ 412,676	\$ 458,110

Note 12—Shareholders' Equity

Share Data: A summary of preferred and common share activity is presented in the following chart.

	Preferred Stock		Common Stock	
	Issued	Treasury Stock	Issued	Treasury Stock
2015:				
Balance at January 1, 2015	—	—	134,218,183	(6,287,907)
Grants of restricted stock				6,648
Forfeitures of restricted stock				(13,950)
Vesting of performance shares				211,287
Issuance of common stock due to exercise of stock options				1,576,485
Treasury stock acquired				(7,340,794)
Retirement of treasury stock			(4,000,000)	4,000,000
Balance at December 31, 2015	—	—	130,218,183	(7,848,231)
2016:				
Grants of restricted stock				12,549
Forfeitures of restricted stock				—
Vesting of performance shares				159,020
Issuance of common stock due to exercise of stock options				2,184,169
Treasury stock acquired				(6,694,582)
Retirement of treasury stock			(3,000,000)	3,000,000
Balance at December 31, 2016	—	—	127,218,183	(9,187,075)
2017:				
Grants of restricted stock				9,135
Vesting of performance shares				119,896
Issuance of common stock due to exercise of stock options				1,661,808
Treasury stock acquired				(5,228,868)
Retirement of treasury stock			(3,000,000)	3,000,000
Balance at December 31, 2017	—	—	124,218,183	(9,625,104)

Acquisition of Common Shares: Torchmark shares are acquired from time to time through open market purchases under the Torchmark stock repurchase program when it is believed to be the best use of Torchmark's excess cash flows. Share repurchases under this program were 4.1 million shares at a cost of \$325 million in 2017, 5.2 million shares at a cost of \$311 million in 2016, and 6.3 million shares at a cost of \$359 million in 2015. When stock options are exercised, proceeds from the exercises are generally used to repurchase approximately the number of shares available with those funds in order to reduce dilution. Shares repurchased for dilution purposes were 1.1 million shares at a cost of \$88 million in 2017, 1.5 million shares at a cost of \$93 million in 2016, and 1.0 million shares at a cost of \$60 million in 2015.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 12—Shareholders' Equity (continued)

Retirement of Treasury Stock: Torchmark retired 3.0 million shares of treasury stock in 2017, 3.0 million in 2016, and 4.0 million in 2015.

Restrictions: Restrictions exist on the flow of funds to Torchmark from its insurance subsidiaries. Statutory regulations require life insurance subsidiaries to maintain certain minimum amounts of capital and surplus. Dividends from insurance subsidiaries of Torchmark are restricted based on regulations by their states of domicile. Additionally, insurance company distributions are generally not permitted in excess of statutory surplus. Subsidiaries are also subject to certain minimum capital requirements. Subsidiaries of Torchmark paid cash dividends to the Parent Company in the amount of \$454 million in 2017, \$438 million in 2016, and \$466 million in 2015. As of December 31, 2017, dividends and transfers from insurance subsidiaries to parent available to be paid in 2018 are limited to the amount of \$315 million without regulatory approval, such that \$940 million was considered restricted net assets of the subsidiaries. Dividends exceeding these limitations may be available during the year pending regulatory approval. While there are no legal restrictions on the payment of dividends to shareholders from Torchmark's retained earnings, retained earnings as of December 31, 2017 were restricted by lenders' covenants which require the Company to maintain and not distribute \$3.5 billion from its total consolidated retained earnings of \$4.8 billion.

Earnings Per Share: A reconciliation of basic and diluted weighted-average shares outstanding used in the computation of basic and diluted earnings per share is as follows:

	Year Ended December 31,		
	2017	2016	2015
Basic weighted average shares outstanding	116,342,529	120,001,191	125,094,628
Weighted average dilutive options outstanding	2,640,965	2,366,594	1,662,607
Diluted weighted average shares outstanding	118,983,494	122,367,785	126,757,235

For the three years ended December 31, 2017, there were no anti-dilutive shares. Income available to common shareholders for basic earnings per share is equivalent to income available to common shareholders for diluted earnings per share.

Note 13—Stock-Based Compensation

Torchmark's stock-based compensation consists of stock options, restricted stock, restricted stock units, and performance shares. Certain employees and directors have been granted fixed equity options to buy shares of Torchmark stock at the market value of the stock on the date of grant, under the provisions of the Torchmark stock option plans. The options are exercisable during the period commencing from the date they vest until expiring according to the terms of the grant. Options generally expire the earlier of employee termination or option contract term, which are either seven or ten year terms. Options generally vest in accordance with the following schedule:

	Contract Period	Shares vested by period					
		6 Months	Year 1	Year 2	Year 3	Year 4	Year 5
Directors	7 years	100%					
Employees	7 years	—%	—%	50%	50%		
Employees ⁽¹⁾	10 years	—%	—%	25%	25%	25%	25%

(1) Grant offered through the Torchmark Corporation 2011 Incentive Plan only.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 13—Stock-Based Compensation (continued)

All employee options vest immediately upon retirement on or after the attainment of age 65, upon death, or disability. Torchmark generally issues shares for the exercise of stock options from treasury stock. The Company generally uses the proceeds from option exercises to buy shares of Torchmark common stock in the open market to reduce the dilution from option exercises.

An analysis of shares available for grant is as follows:

	Available for Grant		
	2017	2016	2015
Balance at January 1,	5,088,461	6,872,282	8,458,593
Options expired and forfeited during year ⁽¹⁾	26,488	8,518	90,371
Restricted stock expired and forfeited during year ⁽²⁾	46,500	—	89,745
Options granted during year ⁽¹⁾	(1,328,513)	(1,306,306)	(1,334,514)
Restricted stock, restricted stock units, and performance shares granted under the Torchmark Corporation 2011 Incentive Plan ⁽²⁾	(868,616)	(486,033)	(431,913)
Balance at December 31,	<u>2,964,320</u>	<u>5,088,461</u>	<u>6,872,282</u>

(1) Plan allows for grant of options such that each grant reduces shares available for grant in a range from 0.85 share to 1 share.

(2) Plan allows for grant of restricted stock such that each stock grant reduces shares available for grant in a range from 3.1 shares to 3.88 shares.

A summary of stock compensation activity for each of the three years ended December 31, 2017 is presented below:

	2017	2016	2015
Stock-based compensation expense recognized ⁽¹⁾	\$ 37,034	\$ 26,326	\$ 28,664
Tax benefit recognized	32,511	27,867	10,033

(1) No stock-based compensation expense was capitalized in any period.

Additional stock compensation information is as follows at December 31:

	2017	2016
Unrecognized compensation ⁽¹⁾	\$ 31,309	\$ 27,334
Weighted average period of expected recognition (in years) ⁽¹⁾	0.86	0.89

(1) Includes restricted stock and performance shares.

No equity awards were cash settled during the three years ended December 31, 2017.

Options: The following table summarizes information about stock options outstanding at December 31, 2017.

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
\$29.59 - \$37.40	1,421,268	2.20	\$ 34.54	1,366,689	\$ 34.42
50.64	1,405,725	6.39	50.64	—	—
50.69 - 51.62	1,090,703	3.69	50.70	958,463	50.70
53.61 - 56.32	1,384,582	4.63	53.65	594,184	53.71
73.92 - 77.26	1,451,523	7.23	77.24	9,643	73.92
\$29.59 - \$77.26	<u>6,753,801</u>	<u>4.89</u>	<u>\$ 53.59</u>	<u>2,928,979</u>	<u>\$ 43.79</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 13—Stock-Based Compensation (continued)

An analysis of option activity for each of the three years ended December 31, 2017 is as follows:

	2017		2016		2015	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding—beginning of year	6,973,591	\$ 44.64	7,734,841	\$ 38.84	7,889,321	\$ 32.91
Granted:						
7-year term	933,286	77.19	834,212	50.78	1,220,751	53.62
10-year term	535,220	77.26	597,225	50.64	296,875	53.61
Exercised	(1,661,808)	36.84	(2,184,169)	28.08	(1,576,485)	22.81
Expired and forfeited	(26,488)	57.94	(8,518)	39.35	(95,621)	48.85
Outstanding—end of year	<u>6,753,801</u>	<u>\$ 53.59</u>	<u>6,973,591</u>	<u>\$ 44.64</u>	<u>7,734,841</u>	<u>\$ 38.84</u>
Exercisable at end of year	<u>2,928,979</u>	<u>\$ 43.79</u>	<u>3,115,847</u>	<u>\$ 36.81</u>	<u>3,774,061</u>	<u>\$ 29.37</u>

Additional information about Torchmark's stock option activity as of December 31, 2017 and 2016 is as follows:

	2017	2016
Outstanding options:		
Weighted-average remaining contractual term (in years)	4.89	4.70
Aggregate intrinsic value	\$ 231,277	\$ 87,286
Exercisable options:		
Weighted-average remaining contractual term (in years)	2.99	2.96
Aggregate intrinsic value	\$ 137,424	\$ 63,395

Selected stock option activity for the three years ended December 31, 2017 is presented below:

	2017	2016	2015
Weighted-average grant-date fair value of options granted (per share)	\$ 12.88	\$ 9.04	\$ 11.97
Intrinsic value of options exercised	70,948	73,995	54,854
Cash received from options exercised	61,215	61,329	35,958
Actual tax benefit received	24,832	25,898	24,470

Additional information concerning Torchmark's unvested options is as follows at December 31:

	2017	2016
Number of shares outstanding	3,824,822	3,857,744
Weighted-average exercise price (per share)	\$ 61.10	\$ 50.97
Weighted-average remaining contractual term (in years).....	6.34	6.11
Aggregate intrinsic value	\$ 113,246	\$ 23,891

Torchmark expects that substantially all unvested options will vest.

Restricted Stock: Restricted stock grants consist of time-vested grants, restricted stock units, and performance shares. Time-vested restricted stock is available to both senior executives and directors. The employee grants generally vest over five years and the director grants vest over six months. Restricted stock units are available only to directors. They

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 13—Stock-Based Compensation (continued)

vest over six months and are not converted to shares until the directors' retirement, death, or disability. Director restricted stock and restricted stock units are generally granted on the first work day of the year. Performance shares are granted to a limited number of senior executives. Performance shares have a three year contract life and are not settled in shares until the termination of the three-year contract period. While the grant specifies a stated target number of shares, the determination of the actual settlement in shares will be based on the achievement of certain performance objectives of Torchmark over the respective three-year contract periods. Certain executive restricted stock and performance share grants contain terms related to age that could accelerate vesting.

Restricted stock units outstanding at each of the year ends 2017, 2016, and 2015 were 120,326, 112,591, and 105,679, respectively. All restricted stock units were fully vested at the end of each year of grant.

Below is the final determination of the performance share grants in 2013 to 2015:

Year of grants	Final settlement of shares	Final settlement date
2013	159,020	February 24, 2016
2014	119,896	February 21, 2017
2015	149,898	February 27, 2018

For the 2016 and 2017 performance share grants, actual shares that could be distributed range from 0 to 335 thousand for the 2016 grants and 0 to 306 thousand shares for the 2017 grants.

A summary of restricted stock grants for each of the years in the three-year period ended December 31, 2017 is presented in the table below.

	2017	2016	2015
Directors restricted stock:			
Shares	9,135	12,549	6,648
Price per share	\$ 73.92	\$ 57.39	\$ 54.16
Aggregate value	\$ 675	\$ 720	\$ 360
Percent vested as of December 31, 2017	100%	85%	100%
Directors restricted stock units (including dividend equivalents):			
Shares	7,735	6,912	7,640
Price per share	\$ 74.45	\$ 56.74	\$ 54.44
Aggregate value	\$ 576	\$ 392	\$ 416
Percent vested as of December 31, 2017	100%	100%	100%
Performance shares:			
Target shares	153,000	167,500	179,500
Target price per share	\$ 77.26	\$ 50.64	\$ 53.61
Assumed adjustment for performance objectives (in shares)	106,084	(35,073)	(58,056)
Aggregate value	\$ 11,821	\$ 8,482	\$ 9,623
Percent vested as of December 31, 2017	—%	—%	—%

Time-vested restricted stock holders, both employees and directors, are entitled to dividend payments on the unvested stock. Restricted stock unit holders are entitled to dividend equivalents. These equivalents are granted in the form of additional restricted stock units and vest immediately upon grant. Dividend equivalents are applicable only to restricted stock units. Performance shareholders are not entitled to dividend equivalents and are not entitled to dividend payments until the shares are vested and settled.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 13—Stock-Based Compensation (continued)

An analysis of unvested restricted stock is as follows:

	Executive Restricted Stock	Executive Performance Shares	Directors Restricted Stock	Directors Restricted Stock Units	Total
2015:					
Balance at January 1, 2015	263,430	556,360	—	—	819,790
Grants	—	179,500	6,648	7,640	193,788
Additional performance shares ⁽¹⁾		(58,056)			(58,056)
Restriction lapses	(61,815)	(211,287)	(6,648)	(7,640)	(287,390)
Forfeitures	(13,950)	(7,500)			(21,450)
Balance at December 31, 2015	187,665	459,017	—	—	646,682
2016:					
Grants	—	167,500	12,549	6,912	186,961
Additional performance shares ⁽¹⁾		(35,073)			(35,073)
Restriction lapses	(130,215)	(159,020)	(10,655)	(6,912)	(306,802)
Forfeitures	—	—			—
Balance at December 31, 2016	57,450	432,424	1,894	—	491,768
2017:					
Grants	—	153,000	9,135	7,735	169,870
Additional performance shares ⁽¹⁾		106,084			106,084
Restriction lapses	(14,700)	(119,896)	(11,029)	(7,735)	(153,360)
Forfeitures	(7,500)	(7,500)			(15,000)
Balance at December 31, 2017	35,250	564,112	—	—	599,362

(1) Estimated additional (reduced) share grants expected due to achievement of performance criteria.

An analysis of the weighted-average grant-date fair values per share of unvested restricted stock is as follows for the year 2017:

	Executive Restricted Stock	Executive Performance Shares	Directors Restricted Stock	Directors Restricted Stock Units
Grant-date fair value per share at January 1, 2017	\$ 38.46	\$ 49.79	\$ 63.39	
Grants	—	77.26	73.92	\$ 73.92
Estimated additional performance shares		71.76		
Restriction lapses	(30.69)	(72.42)	(72.11)	(73.92)
Forfeitures	(37.40)	(43.85)		
Grant-date fair value per share at December 31, 2017	41.93	56.64		

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
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Note 14—Business Segments

Torchmark is organized into four segments: life insurance, supplemental health insurance, annuities, and investments. We also have other administrative expenses reported in "Corporate & Other."

Torchmark's reportable segments are based on the insurance product lines it markets and administers: life insurance, supplemental health insurance, and annuities. These major product lines are set out as reportable segments because of the common characteristics of products within these categories, comparability of margins, and the similarity in regulatory environment and management techniques. There is also an investment segment which manages the investment portfolio, debt, and cash flow for the insurance segments and the corporate function. Torchmark's chief operating decision makers evaluate the overall performance of the operations of the Company in accordance with these segments.

Life insurance products include traditional and interest-sensitive whole life insurance as well as term life insurance. Health insurance products are generally guaranteed-renewable and include Medicare Supplement, critical illness, accident, and limited-benefit supplemental hospital and surgical coverages. Annuities include fixed-benefit contracts.

Torchmark markets its insurance products through a number of distribution channels, each of which sells the products of one or more of Torchmark's insurance segments. The tables below present segment premium revenue by each of Torchmark's distribution channels.

Torchmark Corporation
Premium Income by Distribution Channel

For the Year 2017								
<u>Distribution Channel</u>	Life		Health		Annuity		Total	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
United American Independent...	\$ 12,547	1	\$ 364,128	37	\$ 15	100	\$ 376,690	12
Liberty National Exclusive	274,635	12	196,207	20			470,842	14
American Income Exclusive	999,279	43	89,036	9			1,088,315	33
Family Heritage Exclusive	3,193	—	253,534	26			256,727	8
Direct Response	812,907	35	73,468	8			886,375	27
Other	203,986	9					203,986	6
	<u>\$ 2,306,547</u>	<u>100</u>	<u>\$ 976,373</u>	<u>100</u>	<u>\$ 15</u>	<u>100</u>	<u>\$ 3,282,935</u>	<u>100</u>

For the Year 2016								
<u>Distribution Channel</u>	Life		Health		Annuity		Total	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
United American Independent...	\$ 13,733	1	\$ 355,015	38	\$ 38	100	\$ 368,786	12
Liberty National Exclusive	270,476	12	201,798	21			472,274	15
American Income Exclusive	913,355	42	84,382	9			997,737	32
Family Heritage Exclusive	2,866	—	236,075	25			238,941	8
Direct Response	782,765	36	70,393	7			853,158	27
Other	206,138	9					206,138	6
	<u>\$ 2,189,333</u>	<u>100</u>	<u>\$ 947,663</u>	<u>100</u>	<u>\$ 38</u>	<u>100</u>	<u>\$ 3,137,034</u>	<u>100</u>

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 14—Business Segments (continued)

Distribution Channel	For the Year 2015							
	Life		Health		Annuity		Total	
	Amount	% of Total	Amount	% of Total	Amount	% of Total	Amount	% of Total
United American Independent...	\$ 15,036	1	\$ 345,330	37	\$ 135	100	\$ 360,501	12
Liberty National Exclusive	271,113	13	209,150	23			480,263	16
American Income Exclusive	830,903	40	80,339	9			911,242	30
Family Heritage Exclusive	2,334	—	221,091	24			223,425	8
Direct Response	746,693	36	69,610	7			816,303	27
Other	206,986	10					206,986	7
	<u>\$ 2,073,065</u>	<u>100</u>	<u>\$ 925,520</u>	<u>100</u>	<u>\$ 135</u>	<u>100</u>	<u>\$ 2,998,720</u>	<u>100</u>

Due to the nature of the life insurance industry, Torchmark has no individual or group which would be considered a major customer. Substantially all of Torchmark's business is conducted in the United States.

The measure of profitability established by the chief operating decision makers for insurance segments is underwriting margin before other income and administrative expenses, in accordance with the manner the segments are managed. It essentially represents gross profit margin on insurance products before insurance administrative expenses and consists of premium, less net policy obligations, acquisition expenses, and commissions. Interest credited to net policy liabilities (reserves less deferred acquisition costs) is reflected as a component of the Investment segment in order to match this cost to the investment earnings from the assets supporting the net policy liabilities.

The measure of profitability for the Investment segment is excess investment income, which represents the income earned on the investment portfolio in excess of net policy requirements and financing costs associated with Torchmark's debt. Other than the above-mentioned interest allocations and an intersegment commission, there are no other intersegment revenues or expenses. Expenses directly attributable to corporate operations are included in the "Corporate & Other" category. Stock-based compensation expense is considered a corporate expense by Torchmark management and is included in this category. All other unallocated revenues and expenses on a pretax basis, including insurance administrative expense, are also included in the "Corporate & Other" segment category.

Torchmark holds a sizable investment portfolio to support its insurance liabilities, the yield from which is used to offset policy benefit, acquisition, administrative and tax expenses. This yield or investment income is taken into account when establishing premium rates and profitability expectations of its insurance products. In holding such a portfolio, investments are sold, called, or written down from time to time, resulting in a realized gain or loss. These gains or losses generally occur as a result of disposition due to issuer calls, compliance with Company investment policies, or other reasons often beyond management's control. Unlike investment income, realized gains and losses are incidental to insurance operations, and only overall yields are considered when setting premium rates or insurance product profitability expectations. While these gains and losses are not relevant to segment profitability or core operating results, they can have a material positive or negative result on net income. For these reasons, management removes realized investment gains and losses when it views its segment operations.

Management removes items that are related to prior periods when evaluating the operating results of current periods. Management also removes non-operating items unrelated to its core insurance activities when evaluating those results. Therefore, these items are excluded in its presentation of segment results, because accounting guidance requires that operating segment results be presented as management views its business. With the exception of the administrative settlements noted in the paragraphs above, all of these items are included in "Other operating expense" in the *Consolidated Statements of Operations* for the appropriate year.

In 2017, Torchmark recorded \$8.7 million in administrative settlements (\$5.6 million after tax) where claims were not properly filed or information to support the validity of the claim had not been properly submitted. These administrative settlements were included in "Policyholder benefits" in the *Consolidated Statements of Operations* in 2017.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 14—Business Segments (continued)

As further discussed in *Note 15—Commitments and Contingencies*, the Company received an assessment from various state guaranty fund associations for the liquidation of Penn Treaty and its affiliate. The total estimated assessment for Torchmark's subsidiaries is approximately \$9.6 million of which \$1.8 million is estimated to be unrecoverable. We are anticipating the remaining amount of the assessments to be recovered through premium tax credits. The assessment expenses were considered a non-operational event and therefore were excluded from the core underwriting operations of the Company.

As a result of the Tax Legislation, which is discussed in *Note 1—Significant Accounting Policies*, we recorded a one-time increase in stock-based compensation expense of 3.4 million (\$2.2 million after tax) due to the impact the Tax Legislation had on certain performance based equity awards.

In 2016, Torchmark recorded \$3.8 million in administrative settlements (\$2.5 million after tax) related to benefits paid for deaths occurring in prior years where claims had not been filed. These administrative settlements were included in "Policyholder benefits" in the *Consolidated Statements of Operations* in 2016.

In 2015, Torchmark recorded \$1.4 million in administrative settlements (\$906 thousand after tax) related to a post-closing adjustment on the sale of a former subsidiary. These administrative settlements were included in "Commissions, premium taxes, and non-deferred acquisition costs" in the *Consolidated Statements of Operations* in 2015.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
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Note 14—Business Segments (continued)

The following tables set forth a reconciliation of Torchmark's revenues and operations by segment to its major income statement line items. See *Note 1—Significant Accounting Policies* for additional information concerning reconciling items of segment profits to pretax income.

	For the year 2017						Consolidated
	Life	Health	Annuity	Investment	Corporate & Other	Adjustments	
Revenue:							
Premium	\$2,306,547	\$ 976,373	\$ 15				\$ 3,282,935
Net investment income				\$ 847,885			847,885
Other income					\$ 1,270	\$ (128) ⁽²⁾	1,142
Total revenue	2,306,547	976,373	15	847,885	1,270	(128)	4,131,962
Expenses:							
Policy benefits	1,549,602	628,640	35,836			13,797 ^(3,4)	2,227,875
Required interest on:							
Policy reserves	(607,007)	(77,792)	(49,571)	734,370			—
Deferred acquisition costs	186,236	23,454	690	(210,380)			—
Amortization of acquisition costs	396,268	96,519	2,466			(4,850) ⁽⁴⁾	490,403
Commissions, premium taxes, and non-deferred acquisition costs	177,111	86,044	32			1,673 ^(2,5)	264,860
Insurance administrative expense ⁽¹⁾					210,590		210,590
Parent expense					9,631		9,631
Stock-based compensation expense					33,654	3,380 ⁽⁶⁾	37,034
Interest expense				84,532			84,532
Total expenses	1,702,210	756,865	(10,547)	608,522	253,875	14,000	3,324,925
Subtotal	604,337	219,508	10,562	239,363	(252,605)	(14,128)	807,037
Non-operating items						14,128 ^(3,4,5,6)	14,128
Measure of segment profitability (pretax) ...	\$ 604,337	\$ 219,508	\$ 10,562	\$ 239,363	\$ (252,605)	\$ —	821,165
Deduct applicable income taxes							(247,484)
Net operating income from continuing operations							573,681
Add back income taxes applicable to segment profitability							247,484
Add (deduct) realized investment gains (losses)							23,611
Deduct administrative settlements							(8,659)
Deduct non-operating expenses							(288)
Deduct guaranty fund assessments							(1,801)
Deduct increase in stock-based compensation expense due to Tax Legislation							(3,380)
Income before income taxes per <i>Consolidated Statement of Operations</i>							<u>\$ 830,648</u>

- (1) Administrative expense is not allocated to insurance segments.
(2) Elimination of intersegment commission.
(3) Administrative settlements.
(4) Non-operating expense.
(5) Guaranty fund assessments.
(6) Recognition of a one-time increase in stock-based compensation expense due to Tax Legislation.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
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Note 14—Business Segments (continued)

	For the year 2016						
	Life	Health	Annuity	Investment	Corporate & Other	Adjustments	Consolidated
Revenue:							
Premium	\$2,189,333	\$ 947,663	\$ 38				\$ 3,137,034
Net investment income				\$ 806,903			806,903
Other income					\$ 1,534	\$ (159) ⁽²⁾	1,375
Total revenue	2,189,333	947,663	38	806,903	1,534	(159)	3,945,312
Expenses:							
Policy benefits	1,475,477	612,725	36,751			3,795 ⁽³⁾	2,128,748
Required interest on:							
Policy reserves	(577,827)	(73,382)	(51,131)	702,340			—
Deferred acquisition costs	178,946	23,060	807	(202,813)			—
Amortization of acquisition costs	374,499	90,385	4,179				469,063
Commissions, premium taxes, and non- deferred acquisition costs	164,476	84,819	38			(159) ⁽²⁾	249,174
Insurance administrative expense ⁽¹⁾					196,598	553 ⁽⁴⁾	197,151
Parent expense					8,587		8,587
Stock-based compensation expense					26,326		26,326
Interest expense				83,345			83,345
Total expenses	1,615,571	737,607	(9,356)	582,872	231,511	4,189	3,162,394
Subtotal	573,762	210,056	9,394	224,031	(229,977)	(4,348)	782,918
Non-operating items						4,348 ^(3,4)	4,348
Measure of segment profitability (pretax) ...	\$ 573,762	\$ 210,056	\$ 9,394	\$ 224,031	\$ (229,977)	\$ —	787,266
Deduct applicable income taxes							(237,906)
Net operating income from continuing operations							549,360
Add back income taxes applicable to segment profitability							237,906
Add (deduct) realized investment gains (losses)							(10,683)
Deduct administrative settlements							(3,795)
Deduct non-operating fees							(553)
Income before income taxes per <i>Consolidated Statement of Operations</i>							<u>\$ 772,235</u>

(1) Administrative expense is not allocated to insurance segments.

(2) Elimination of intersegment commission.

(3) Administrative settlements.

(4) Non-operating fees.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 14—Business Segments (continued)

	For the Year 2015						Consolidated
	Life	Health	Annuity	Investment	Corporate & Other	Adjustments	
Revenue:							
Premium	\$2,073,065	\$ 925,520	\$ 135				\$ 2,998,720
Net investment income				\$ 773,951			773,951
Other income					\$ 2,379	\$ (194) ⁽²⁾	2,185
Total revenue	2,073,065	925,520	135	773,951	2,379	(194)	3,774,856
Expenses:							
Policy benefits	1,374,608	602,610	38,994				2,016,212
Required interest on:							
Policy reserves	(552,298)	(69,057)	(53,295)	674,650			—
Deferred acquisition costs	172,947	22,760	1,138	(196,845)			—
Amortization of acquisition costs	353,595	83,341	8,689				445,625
Commissions, premium taxes, and non-deferred acquisition costs	154,811	81,489	41			1,200 ^(2,3)	237,541
Insurance administrative expense ⁽¹⁾					186,191		186,191
Parent expense					9,003		9,003
Stock-based compensation expense					28,664		28,664
Interest expense				76,642			76,642
Total expenses	1,503,663	721,143	(4,433)	554,447	223,858	1,200	2,999,878
Subtotal	569,402	204,377	4,568	219,504	(221,479)	(1,394)	774,978
Non-operating items						1,394 ⁽³⁾	1,394
Measure of segment profitability (pretax) ...	\$ 569,402	\$ 204,377	\$ 4,568	\$ 219,504	\$ (221,479)	\$ —	776,372
Deduct applicable income taxes							(253,459)
Net operating income from continuing operations							522,913
Add back income taxes applicable to segment profitability							253,459
Add (deduct) realized investment gains (losses)							(8,791)
Deduct administrative settlements							(1,394)
Income before income taxes per <i>Consolidated Statement of Operations</i>							\$ 766,187

(1) Administrative expense is not allocated to insurance segments.

(2) Elimination of intersegment commission.

(3) Administrative settlements.

Assets for each segment are reported based on a specific identification basis. The insurance segments' assets contain DAC. The investment segment includes the investment portfolio, cash, and accrued investment income. Goodwill is assigned to the insurance segments at the time of purchase. All other assets are included in the Other category. The table below reconciles segment assets to total assets as reported in the consolidated financial statements.

Assets by Segment

	At December 31, 2017					Consolidated
	Life	Health	Annuity	Investment	Other	
Cash and invested assets				\$ 17,853,047		\$ 17,853,047
Accrued investment income .				233,453		233,453
Deferred acquisition costs	\$ 3,423,296	\$ 529,068	\$ 5,699			3,958,063
Goodwill	309,609	131,982				441,591
Other assets					\$ 988,831	988,831
Total assets	\$ 3,732,905	\$ 661,050	\$ 5,699	\$ 18,086,500	\$ 988,831	\$ 23,474,985

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
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Note 14—Business Segments (continued)

	At December 31, 2016					Consolidated
	Life	Health	Annuity	Investment	Other	
Cash and invested assets				\$ 15,955,891		\$ 15,955,891
Accrued investment income .				223,148		223,148
Deferred acquisition costs	\$ 3,261,220	\$ 512,701	\$ 9,237			3,783,158
Goodwill	309,609	131,982				441,591
Other assets					\$ 1,032,299	1,032,299
Total assets	\$ 3,570,829	\$ 644,683	\$ 9,237	\$ 16,179,039	\$ 1,032,299	\$ 21,436,087

Liabilities for each segment are reported also on a specific identification basis similar to the assets. The insurance segments' liabilities contain future policy benefits, unearned and advance premiums, and policy claims and other benefits payable. Other policyholders' funds are included in Other as well as current and deferred income taxes payable. Debt represents both short and long-term.

Liabilities by Segment

	At December 31, 2017					Consolidated
	Life	Health	Annuity	Investment	Other	
Future policy benefits	\$ 10,353,286	\$ 1,831,338	\$ 1,254,848			\$ 13,439,472
Unearned and advance premiums	16,927	44,503				61,430
Policy claims and other benefits payable	186,429	146,865				333,294
Debt				\$ 1,460,268		1,460,268
Other					\$ 1,949,100	1,949,100
Total liabilities	\$ 10,556,642	\$ 2,022,706	\$ 1,254,848	\$ 1,460,268	\$ 1,949,100	\$ 17,243,564

	At December 31, 2016					Consolidated
	Life	Health	Annuity	Investment	Other	
Future policy benefits	\$ 9,825,776	\$ 1,706,870	\$ 1,293,191			\$ 12,825,837
Unearned and advance premiums	16,828	47,189				64,017
Policy claims and other benefits payable	156,437	143,128				299,565
Debt				\$ 1,397,640		1,397,640
Other					\$ 2,282,167	2,282,167
Total liabilities	\$ 9,999,041	\$ 1,897,187	\$ 1,293,191	\$ 1,397,640	\$ 2,282,167	\$ 16,869,226

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 15—Commitments and Contingencies

Reinsurance: Insurance affiliates of Torchmark reinsure that portion of insurance risk which is in excess of their retention limits. Retention limits for ordinary life insurance range up to \$2 million per life. Life insurance ceded represented 0.4% of total life insurance in force at December 31, 2017. Insurance ceded on life and accident and health products represented 0.2% of premium income for 2017. Torchmark would be liable for the reinsured risks ceded to other companies to the extent that such reinsuring companies are unable to meet their obligations.

Insurance affiliates also assume insurance risks of other external companies. Life reinsurance assumed represented 1.8% of life insurance in force at December 31, 2017 and reinsurance assumed on life and accident and health products represented 0.7% of premium income for 2017.

Leases: Torchmark leases office space, office equipment, and aviation equipment under a variety of operating lease arrangements. The Company does not have any capital leases.

Rental expense for operating leases for each of the three years ended December 31, 2017 is as follows:

	Year Ended December 31,		
	2017	2016	2015
Rental expense	\$ 6,446	\$ 6,520	\$ 6,722

Future minimum rental commitments required under operating leases having remaining noncancelable lease terms in excess of one year at December 31, 2017 were as follows:

	Year Ended December 31,					
	2018	2019	2020	2021	2022	Thereafter
Operating lease commitments	\$ 3,483	\$ 3,298	\$ 3,124	\$ 2,886	\$ 1,943	\$ 1,830

Purchase Commitments: Torchmark has various long-term noncancelable purchase commitments as well as commitments to provide capital for low-income housing tax credit interests. See further discussion related to tax credits in *Note 1—Significant Accounting Policies*.

	Year Ended December 31,					
	2018	2019	2020	2021	2022	Thereafter
Purchase commitments	\$27,326	\$ 9,198	\$ 3,257	\$ 2,213	\$ 2,169	\$ 246,836

Investments: As of December 31, 2017, Torchmark is committed to purchase \$210 million of commercial mortgage loan participations from a third party.

Guarantees: At December 31, 2017, Torchmark had in place four guarantee agreements, of which were either Parent Company guarantees of subsidiary obligations to a third party, or Parent Company guarantees of obligations between wholly-owned subsidiaries. As of December 31, 2017, Torchmark had no liability with respect to these guarantees.

Letters of Credit: Torchmark has guaranteed letters of credit in connection with its credit facility with a group of banks as disclosed in *Note 11—Debt*. The letters of credit were issued by TMK Re, Ltd., a wholly-owned subsidiary, to secure TMK Re, Ltd.'s obligation for claims on certain policies reinsured by TMK Re, Ltd. that were sold by other Torchmark insurance companies. These letters of credit facilitate TMK Re, Ltd.'s ability to reinsure the business of Torchmark's insurance carriers. The agreement expires in 2021. The maximum amount of letters of credit available is \$250 million. The Torchmark Parent Company would be liable to the extent that TMK Re, Ltd. does not pay the reinsured party. Letters of credit outstanding were \$177 million at December 31, 2017 and 2016.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands except per share data)

Note 15—Commitments and Contingencies (continued)

Equipment leases: Torchmark has guaranteed performance of certain subsidiaries as lessees under three leasing arrangements which include two for aviation equipment and one for computer software, furniture, and equipment. One aviation lease expires in August 2022 and the second expires in September 2024. The office equipment lease expired in December 2017. At December 31, 2017, total remaining undiscounted payments under the leases were approximately \$10 million. The Torchmark Parent Company would be responsible for any subsidiary obligation in the event the subsidiary did not make payments or otherwise perform under the terms of the lease.

Unclaimed Property Audits: Torchmark subsidiaries are currently the subject of audits regarding the identification, reporting and escheatment of unclaimed property arising from life insurance policies and a limited number of annuity contracts. These audits are being conducted by private entities that have contracted with forty-seven states through their respective Departments of Revenue, and have not resulted in any financial assessment from any state nor indicated any liability. The audits are wide-ranging and seek large amounts of data regarding claims handling, procedures, and payments of contract benefits arising from unreported death claims. No estimate of range can be made at this time for loss contingencies related to possible administrative penalties or amounts that could be payable to the states for the escheatment of abandoned property.

Litigation: Torchmark and its subsidiaries, in common with the insurance industry in general, are subject to litigation, including claims involving tax matters, alleged breaches of contract, torts, including bad faith and fraud claims based on alleged wrongful or fraudulent acts of agents of Torchmark's subsidiaries, employment discrimination, and miscellaneous other causes of action. Based upon information presently available, and in light of legal and other factual defenses available to Torchmark and its subsidiaries, management does not believe that such litigation will have a material adverse effect on Torchmark's financial condition, future operating results or liquidity; however, assessing the eventual outcome of litigation necessarily involves forward-looking speculation as to judgments to be made by judges, juries and appellate courts in the future. This bespeaks caution, particularly in states with reputations for high punitive damage verdicts. Torchmark's management recognizes that large punitive damage awards bearing little or no relation to actual damages continue to be awarded by juries in jurisdictions in which Torchmark and its subsidiaries have substantial business, creating the potential for unpredictable material adverse judgments in any given punitive damage suit.

On February 1, 2018, a putative class action litigation was filed against American Income Life Insurance Company in U.S. District Court for the Northern District of Texas, Dallas Division (*Bruce v. American Income Life Insurance Company, et al.*, Case No. 3:18-cv-00258-G). The plaintiff, a former insurance sales agent of American Income who is suing on behalf of all current and former American Income sales agents contracted through State General Agent Stephen Jubrey's agency office at any time since January 31, 2015 through the final disposition of this matter, asserts that such agents are employees rather than independent contractors as they are classified by American Income. He alleges failure to pay minimum wages, overtime wages and other applicable monies in accordance with the Fair Labor Standards Act. The plaintiff seeks, in a jury trial, actual and punitive damages, pre- and post-judgment interest, attorney fees, costs and other relief, including injunctive relief.

With respect to its current litigation, at this time management believes that the possibility of a material judgment adverse to Torchmark is remote, and no estimate of range can be made for loss contingencies that are at least reasonably possible but not accrued.

Guaranty Fund Assessment: In 2017, the Commonwealth Court of Pennsylvania issued orders placing Penn Treaty Network America Insurance Company (Penn Treaty) and affiliate American Network Insurance Company (ANIC) in liquidation due to financial difficulties. In such instances, the various state guaranty fund associations employ funding mechanisms, through assessments to their member companies, to cover the obligations of the insolvent entities. Consequently, the Company continues to receive guaranty fund assessments from the state associations related to these companies. The Company has projected its share of the ultimate assessments from these insolvencies based on assumptions about future events and its market share of premiums by state. The total estimated assessment for Torchmark's subsidiaries is approximately \$9.6 million of which \$7.8 million is estimated to be recoverable through state premium tax credit offsets. We anticipate the remaining \$1.8 million will be unrecoverable.

TORCHMARK CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Dollar amounts in thousands, except per share data)

Note 16—Selected Quarterly Data (Unaudited)

The following is an unaudited summary of quarterly results for the two years ended December 31, 2017. The information includes all adjustments (consisting of normal accruals) which management considers necessary for a fair presentation of the results of operations for these periods.

	Three Months Ended			
	March 31,	June 30,	September 30,	December 31,
2017:				
Premium income	\$ 820,631	\$ 816,614	\$ 819,217	\$ 826,473
Net investment income	208,282	212,776	213,872	212,955
Realized investment gains (losses)	(5,748)	(705)	12,595	17,469
Total revenue	1,023,581	1,029,078	1,046,015	1,056,899
Policyholder benefits	557,776	556,415	551,219	562,465
Amortization of deferred acquisition costs	125,908	122,121	122,334	120,040
Pretax income from continuing operations	191,741	201,926	220,610	216,371
Income from continuing operations	137,178	140,363	153,346	1,027,376
Income from discontinued operations	(3,637)	(90)	(12)	(30)
Net income	133,541	140,273	153,334	1,027,346
Basic net income per common share:				
Continuing operations	1.16	1.20	1.32	8.93
Discontinued operations	(0.03)	—	—	—
Total basic net income per common share	1.13	1.20	1.32	8.93
Diluted net income per common share:				
Continuing operations	1.14	1.18	1.29	8.71
Discontinued operations	(0.03)	—	—	—
Total diluted net income per common share ..	1.11	1.18	1.29	8.71

	Three Months Ended			
	March 31,	June 30,	September 30,	December 31,
2016:				
Premium income	\$ 779,860	\$ 785,855	\$ 783,411	\$ 787,908
Net investment income	197,053	201,642	202,720	205,488
Realized investment gains (losses)	293	4,005	3,482	(18,463)
Total revenue	977,627	991,884	989,773	975,345
Policyholder benefits	524,973	531,485	532,152	540,138
Amortization of deferred acquisition costs	118,806	117,245	116,821	116,191
Pretax income from continuing operations	195,448	199,344	201,461	175,982
Income from continuing operations	133,574	139,294	141,910	124,812
Income from discontinued operations	(9,541)	(865)	9,959	10,636
Net income	124,033	138,429	151,869	135,448
Basic net income per common share:				
Continuing operations	1.10	1.16	1.19	1.05
Discontinued operations	(0.08)	(0.01)	0.08	0.09
Total basic net income per common share	1.02	1.15	1.27	1.14
Diluted net income per common share:				
Continuing operations	1.08	1.13	1.16	1.03
Discontinued operations	(0.07)	—	0.09	0.09
Total diluted net income per common share ..	1.01	1.13	1.25	1.12

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

No disagreements with accountants on any matter of accounting principles or practices or financial statement disclosure have been reported on a Form 8-K within the twenty-four months prior to the date of the most recent financial statements.

Item 9A. Controls and Procedures

Torchmark, under the direction of the Co-Chairmen and Chief Executive Officers and the Executive Vice President and Chief Financial Officer, has established disclosure controls and procedures that are designed to ensure that information required to be disclosed by Torchmark in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. The disclosure controls and procedures are also intended to ensure that such information is accumulated and communicated to Torchmark's management, including the Co-Chairmen and Chief Executive Officers and the Executive Vice President and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

As of the end of the fiscal year completed December 31, 2017, an evaluation was performed under the supervision and with the participation of Torchmark management, including the Co-Chairmen and Chief Executive Officers and the Executive Vice President and Chief Financial Officer, of Torchmark's disclosure controls and procedures (as those terms are defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based upon their evaluation, the Co-Chairmen and Chief Executive Officers and the Executive Vice President and Chief Financial Officer have concluded that Torchmark's disclosure controls and procedures are effective as of the date of this Form 10-K. In compliance with Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350), each of these officers executed a Certification included as an exhibit to this Form 10-K.

As of the quarter ended December 31, 2017, there have not been any changes in Torchmark's internal control over financial reporting or in other factors that could significantly affect this control over financial reporting subsequent to the date of their evaluation which have materially affected, or are reasonably likely to materially affect, Torchmark's internal control over financial reporting. No material weaknesses in such internal controls were identified in the evaluation and as a consequence, no corrective action was required to be taken.

Item 9B. Other Information

There were no items required.

Management's Report on Internal Control over Financial Reporting

Management at Torchmark Corporation is responsible for establishing and maintaining adequate internal control over financial reporting for the Company and for assessing the effectiveness of internal control on an annual basis. As a framework for assessing internal control over financial reporting, the Company utilizes the criteria for effective internal control over financial reporting described in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

There are inherent limitations in the effectiveness of any internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

Management evaluated the Company's internal control over financial reporting, and based on its assessment, determined that the Company's internal control over financial reporting was effective as of December 31, 2017. The Company's independent registered public accounting firm has issued an attestation report on the Company's internal control over financial reporting as stated in their report which is included herein.

/s/ Gary L. Coleman

Gary L. Coleman
Co-Chairman and Chief Executive Officer

/s/ Larry M. Hutchison

Larry M. Hutchison
Co-Chairman and Chief Executive Officer

/s/ Frank M. Svoboda

Frank M. Svoboda
Executive Vice President and Chief Financial Officer

February 26, 2018

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders and the Board of Directors of Torchmark Corporation (McKinney, Texas)

Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of Torchmark Corporation and subsidiaries (Torchmark) as of December 31, 2017, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, Torchmark maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control - Integrated Framework* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements and financial statement schedules as of and for the year ended December 31, 2017 of Torchmark and our report dated February 26, 2018 expressed an unqualified opinion on those financial statements and financial statement schedules.

Basis for Opinion

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

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

Definition and Limitations of Internal Control over Financial Reporting

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

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

/s/ DELOITTE & TOUCHE LLP

Dallas, Texas

February 26, 2018

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Information required by this item is incorporated by reference from the sections entitled “Election of Directors,” “Profiles of Director Nominees,” “Executive Officers,” “Audit Committee Report,” “Governance Guidelines and Codes of Ethics,” “Director Qualification Standards,” “Procedures for Director Nominations by Shareholders,” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Proxy Statement for the Annual Meeting of Shareholders to be held April 26, 2018 (the Proxy Statement), which is to be filed with the Securities and Exchange Commission (SEC).

Item 11. Executive Compensation

Information required by this item is incorporated by reference from the sections entitled “Compensation Discussion and Analysis,” “Compensation Committee Report,” “Summary Compensation Table,” “2017 Grants of Plan-based Awards,” “Outstanding Equity Awards at Fiscal Year End 2017,” “Option Exercises and Stock Vested during Fiscal Year Ended December 31, 2017,” “Pension Benefits at December 31, 2017,” “Potential Payments upon Termination or Change in Control,” “2017 Director Compensation,” “Payments to Directors” and “Compensation Committee Interlocks and Insider Participation” in the Proxy Statement, which is to be filed with the SEC.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

(a) Equity Compensation Plan Information as of December 31, 2017

<u>Plan Category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants, and rights</u>	<u>Weighted-average exercise price of outstanding options, warrants, and rights</u>	<u>Number of securities remaining available for future issuance under equity compensation plans</u>
Equity compensation plans approved by security holders.....	6,753,801	\$ 53.59	2,964,320
Equity compensation plans not approved by security holders.....	—	—	—
Total	<u>6,753,801</u>	<u>\$ 53.59</u>	<u>2,964,320</u>

(b) Security ownership of certain beneficial owners:

Information required by this item is incorporated by reference from the section entitled “Principal Shareholders” in the Proxy Statement, which is to be filed with the SEC.

(c) Security ownership of management:

Information required by this item is incorporated by reference from the section entitled “Stock Ownership” in the Proxy Statement, which is to be filed with the SEC.

(d) Changes in control:

Torchmark knows of no arrangements, including any pledges by any person of its securities, the operation of which may at a subsequent date result in a change of control.

Item 13. Certain Relationships and Related Transactions and Director Independence

Information required by this item is incorporated by reference from the sections entitled “Related Party Transaction Policy and Transactions” and “Director Independence Determinations” in the Proxy Statement, which is to be filed with the SEC.

Item 14. Principal Accountant Fees and Services

Information required by this Item is incorporated by reference from the section entitled “Principal Accounting Firm Fees” and “Pre-approval Policy for Accounting Fees” in the Proxy Statement, which is to be filed with the SEC.

PART IV

Item 15. Exhibits and Financial Statement Schedules

Index of documents filed as a part of this report:

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Consolidated Statements of Comprehensive Income for each of the three years in the period ended December 31, 2017	54
Consolidated Statements of Shareholders' Equity for each of the three years in the period ended December 31, 2017	55
Consolidated Statements of Cash Flows for each of the three years in the period ended December 31, 2017	56
Notes to Consolidated Financial Statements	57
Schedules Supporting Financial Statements for each of the three years in the period ended December 31, 2017:	
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Schedules not referred to have been omitted as inapplicable or not required by Regulation S-X.	

EXHIBITS

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Report

- 3.1 Restated Certificate of Incorporation of Torchmark Corporation, filed with the Delaware Secretary of State on April 30, 2010 (incorporated by reference from Exhibit 3.1.2 to Form 8-K dated May 5, 2010)
- 3.2 Amended and Restated By-Laws of Torchmark Corporation, as amended April 20, 2012 (incorporated by reference from Exhibit 3.2 to Form 8-K dated April 24, 2012)
- 4.1 Trust Indenture dated as of February 1, 1987 between Torchmark Corporation and Morgan Guaranty Trust Company of New York, as Trustee (incorporated by reference from Exhibit 4(b) to Form S-3 for \$300,000,000 of Torchmark Corporation Debt Securities and Warrants (Registration No. 33-11816))
- 4.2 Supplemental Indenture, dated as of December 14, 2001, between Torchmark, BankOne Trust Company, National Association and The Bank of New York, supplementing the Indenture Agreement dated February 1, 1987 (incorporated herein by reference to Exhibit 4(b) to Torchmark's Registration Statement on Form S-3 (File No. 33-11716), and defining the rights of the 6 1/4% Senior Notes (incorporated by reference from Exhibit 4.1 to Form 8-K dated December 14, 2001)
- 4.3 Third Supplemental Indenture dated as of June 30, 2009 between Torchmark Corporation and The Bank of New York Mellon Trust Company, N.A. (incorporated by reference from Exhibit 4 to Form 10-Q for the quarter ended June 30, 2009)
- 4.4 Fourth Supplemental Indenture dated as of September 24, 2012 between Torchmark Corporation and The Bank of New York Mellon Trust Company, N.A., as Trustee, supplementing the Indenture dated February 1, 1987 (incorporated by reference from Exhibit 4.2 to Form 8-K dated September 24, 2012)
- 4.5 Junior Subordinated Indenture, dated November 2, 2001, between Torchmark Corporation and The Bank of New York defining the rights of the 7 3/4% Junior Subordinated Debentures (incorporated by reference from Exhibit 4.3 to Form 8-K dated November 2, 2001)
- 4.6 Second Supplemental Indenture dated as of April 5, 2016 between Torchmark Corporation and The Bank of New York Mellon Trust Company of New York, N.A., as Trustee, supplementing the Junior Subordinated Indenture dated as of November 2, 2011 (incorporated by reference from Exhibit 4.3 to Form 8-K dated April 5, 2016)
- 4.7 Third Supplemental Indenture dated as of November 17, 2017 between Torchmark Corporation and Regions Bank, as Trustee, supplementing the Junior Subordinated Indenture dated as of November 2, 2011 (incorporated by reference from Exhibit 4.4 to Form 8-K dated November 17, 2017)
- 4.8 Certificate and Declaration of Trust of SAFC Statutory Trust I dated February 16, 2006 (incorporated by reference from Exhibit 4.9 to Form 10-K for the fiscal year ended December 31, 2012)
- 4.9 Amended and Restated Declaration of Trust of SAFC Statutory Trust I dated March 1, 2006 (incorporated by reference from Exhibit 4.10 to Form 10-K for the fiscal year ended December 31, 2012)
- 4.10 Indenture dated as of March 1, 2006 for Fixed/Floating Rate Junior Subordinated Deferrable Interest Debentures due 2036 between Southwestern American Financial Corporation and Wilmington Trust Company (incorporated by reference from Exhibit 4.11 to Form 10-K for the fiscal year ended December 31, 2012)
- 10.1 Torchmark Corporation Restated Deferred Compensation Plan for Directors, Advisory Directors, Directors Emeritus and Officers, as amended (incorporated by reference from Exhibit 10(e) to Form 10-K for the fiscal year ended December 31, 1992)*
- 10.2 Amendment One to the Torchmark Corporation Restated Deferred Compensation Plan for Directors, Advisory Directors, Directors Emeritus and Officers (incorporated by reference from Exhibit 10.54 to Form 10-K for the fiscal year ended December 31, 2008)*

- 10.3 Amendment Two to the Torchmark Corporation Restated Deferred Compensation Plan (incorporated by reference from Exhibit 10.55 to Form 10-K for the fiscal year ended December 31, 2008)*
- 10.4 Form of Retirement Life Insurance Benefit Agreement (\$1,995,000 face amount limit) (incorporated by reference from Exhibit 10(z) to Form 10-K for the fiscal year ended December 31, 2001)*
- 10.5 Form of Retirement Life Insurance Benefit Agreement (\$495,000 face amount limit) (incorporated by reference from Exhibit 10(aa) to Form 10-K for the fiscal year ended December 31, 2001)*
- 10.6 Torchmark Corporation Supplemental Executive Retirement Plan (incorporated by reference from Exhibit 10.1 to Form 8-K dated January 25, 2007)*
- 10.7 Amendment No. 1 to the Torchmark Corporation Supplemental Executive Retirement Plan (incorporated by reference from Exhibit 10.53 to Form 10-K for the fiscal year ended December 31, 2007)*
- 10.8 Amendment No. 2 to the Torchmark Corporation Supplemental Executive Retirement Plan (incorporated by reference from Exhibit 10.54 to Form 10-K for the fiscal year ended December 31, 2007)*
- 10.9 Amendment Three to the Torchmark Corporation Supplemental Executive Retirement Plan (incorporated by reference from Exhibit 10.53 to Form 10-K for the fiscal year ended December 31, 2008)*
- 10.10 Amendment Five to the Torchmark Corporation Supplemental Executive Retirement Plan (incorporated by reference to Exhibit 10.1 to Form 8-K dated May 5, 2015)*
- 10.11 Torchmark Corporation Non-Employee Director Compensation Plan, as amended and restated (incorporated by reference from Exhibit 10.1 to Form 8-K dated April 29, 2008)*
- 10.12 Form of Restricted Stock Award Notice under Torchmark Corporation Non-Employee Director Compensation Plan (incorporated by reference from Exhibit 10.57 to Form 10-K for the fiscal year ended December 31, 2007)*
- 10.13 Form of Restricted Stock Unit Award Notice under Torchmark Corporation Non-Employee Director Compensation Plan (incorporated by reference from Exhibit 10.58 to Form 10-K for the fiscal year ended December 31, 2007)*
- 10.14 Receivables Purchase Agreement dated as of December 31, 2008 among ALLIC Receivables Corporation, American Income Life Insurance Company and TMK Re, Ltd. (incorporated by reference from Exhibit 10.1 to Form 8-K dated January 6, 2009)
- 10.15 Amendment No.1 to Receivables Purchase Agreement dated as of December 31, 2008 among ALLIC Receivables Corporation, American Income Life Insurance Company, and TMK Re, Ltd. (incorporated by reference to Exhibit 10.58 to Form 10-K for the fiscal year ended December 31, 2013)
- 10.16 Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.1 to Form 8-K dated May 4, 2011)*
- 10.17 First Amendment to Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.1 to Form 8-K dated April 29, 2014)*
- 10.18 Form of Restricted Stock Award (Executive) under Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.2 to Form 8-K dated May 4, 2011)*
- 10.19 Form of Restricted Stock Award (Special) under Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.3 to Form 8-K dated May 4, 2011)*
- 10.20 Form of Ten year Stock Option under Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.4 to Form 8-K dated May 4, 2011)*

- 10.21 Form of Seven year Stock Option under Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.5 to Form 8-K dated May 4, 2011)*
- 10.22 Form of Performance Share Award under Torchmark Corporation 2011 Incentive Plan (incorporated by reference from Exhibit 10.1 to Form 8-K dated February 27, 2012)*
- 10.23 Form of Seven Year Stock Option Grant Agreement under Torchmark Corporation 2011 Incentive Plan, as amended with Non-Compete, Non-Solicit and Confidentiality Provisions (incorporated by reference from Exhibit 10.75 to Form 10-K for the fiscal year ended December 31, 2016)*
- 10.24 Form of Ten Year Stock Option Grant Agreement under Torchmark Corporation 2011 Incentive Plan, as amended with Non-Compete, Non-Solicit and Confidentiality Provisions (incorporated by reference from Exhibit 10.76 to Form 10-K for the fiscal year ended December 31, 2016)*
- 10.25 Form of Performance Share Award Certificate under Torchmark Corporation 2011 Incentive Plan, as amended with Non-Compete, Non-Solicit and Confidentiality Provisions (incorporated by reference from Exhibit 10.77 to Form 10-K for the fiscal year ended December 31, 2016)*
- 10.26 Form of Seven Year Stock Option Grant Agreement (Special) under Torchmark Corporation 2011 Incentive Plan, as amended with Non-Compete, Non-Solicit and Confidentiality Provisions (incorporated by reference from Exhibit 10.78 to Form 10-K for the fiscal year ended December 31, 2016) *
- 10.27 Torchmark Corporation Amended 2011 Non-Employee Director Compensation Plan, effective January, 2017 (incorporated by reference to Exhibit 10. 55 to Form 10-K for the fiscal year ended December 31, 2016)
- 10.28 Form of Stock Option under Torchmark Corporation 2011 Non-Employee Director Compensation Plan (incorporated by reference from Exhibit 10.57 to Form 10-K for fiscal year ended December 31,2010)*
- 10.29 Form of Restricted Stock Award Notice under Torchmark Corporation 2011 Non-Employee Director Compensation Plan (incorporated by reference from Exhibit 10.58 to Form 10-K for fiscal year ended December 31, 2010)*
- 10.30 Form of Restricted Stock Unit Award Notice under Torchmark Corporation 2011 Non-Employee Director Compensation Plan (incorporated by reference from Exhibit 10.59 to Form 10-K for fiscal year ended December 31, 2010)*
- 10.31 Torchmark Corporation 2013 Management Incentive Plan effective as of January 1, 2013 (incorporated by reference from Exhibit 10.1 to Form 8-K dated April 30, 2013)*
- 10.32 The Torchmark Corporation Amended and Restated Pension Plan Generally Effective as of January 1, 2014* (incorporated by reference from Exhibit 10.14 to Form 10-K for the fiscal year ended December 31, 2015)
- 10.33 Torchmark Corporation Pension Plan 2016 Amendment to Limit Eligibility (effective December 31, 2016) (incorporated by reference to Exhibit 10.80 to Form 10-K for the fiscal year ended December 31, 2016)*
- 10.34 The Torchmark Corporation Savings and Investment Plan (amended and restated as of January 1, 2014)* (incorporated by reference from Exhibit 10.16 to From 10-K for the fiscal year ended December 31, 2015)
- 10.35 Torchmark Corporation Savings and Investment Plan 2016 Amendment Number One* (incorporated by reference from Exhibit 10.2 to Form 8-K dated May 17, 2016)
- 10.36 2016 Amendment to the Torchmark Corporation Savings and Investment Plan (effective December 31, 2016) (incorporated by reference from Exhibit 10-79 to Form 10-K for the fiscal year ended December 31, 2016)*
- 10.37 Payments to Directors (incorporated by reference from Exhibit 10.23 to Form 10-K for the fiscal year ended December 31, 2016)*

10.38	Second Amended and Restated Credit Agreement dated as of May 17, 2016 among Torchmark Corporation, as the Borrower, TMK Re, Ltd., as a Loan Party, Wells Fargo Bank, National Association, as Administrative Agent, Swing Line Lender and L/C Administrator and the other lenders party thereto (incorporated by reference from Exhibit 10.1 to Form 8-K dated May 16, 2016)	
12	Statement re computation of ratios	
20	Proxy Statement for Annual Meeting of Stockholders to be held April 27, 2017**	
21	Subsidiaries of the registrant	122
23	Consent of Deloitte & Touche LLP	
24	Powers of attorney	
31.1	Rule 13a-14(a)/15d-14(a) Certification by Gary L. Coleman	
31.2	Rule 13a-14(a)/15d-14(a) Certification by Larry M. Hutchison	
31.3	Rule 13a-14(a)/15d-14(a) Certification by Frank M. Svoboda	
32.1	Section 1350 Certification by Gary L. Coleman, Larry M. Hutchison and Frank M. Svoboda	
101	Interactive Data File	

* Compensatory plan or arrangement.

** To be filed with the Securities and Exchange Commission within 120 days after the fiscal year ended December 31, 2017.

Exhibit 21. Subsidiaries of the Registrant

The following table lists subsidiaries of the registrant which meet the definition of “significant subsidiary” according to Regulation S-X:

Company	State of Incorporation	Name Under Which Company Does Business
American Income Life Insurance Company	Indiana	American Income Life Insurance Company
Globe Life And Accident Insurance Company	Nebraska	Globe Life And Accident Insurance Company
Liberty National Life Insurance Company	Nebraska	Liberty National Life Insurance Company

While United American Life Insurance Company and Family Heritage Life Insurance Company of America do not qualify as significant subsidiaries in accordance with Regulation S-X, management views these subsidiaries as significant to our operations.

All other exhibits required by Regulation S-K are listed as to location in the “Index of documents filed as a part of this report” in this report. Exhibits not referred to have been omitted as inapplicable or not required.

TORCHMARK CORPORATION
(PARENT COMPANY)
SCHEDULE II. CONDENSED FINANCIAL INFORMATION OF REGISTRANT
CONDENSED BALANCE SHEETS
(Dollar amounts in thousands)

	December 31,	
	2017	2016
Assets:		
Investments:		
Long-term investments	\$ 35,562	\$ 33,586
Short-term investments	5,624	—
Total investments	41,186	33,586
Cash	1,008	—
Investment in affiliates	7,763,704	6,004,429
Due from affiliates	95,920	96,005
Taxes receivable from affiliates	63,099	88,406
Other assets	135,616	119,801
Total assets	\$ 8,100,533	\$ 6,342,227
Liabilities and shareholders' equity:		
Liabilities:		
Short-term debt	\$ 328,067	\$ 264,475
Long-term debt	1,281,971	1,282,891
Due to affiliates	8,002	—
Other liabilities	251,072	228,000
Total liabilities	1,869,112	1,775,366
Shareholders' equity:		
Preferred stock	351	351
Common stock	124,218	127,218
Additional paid-in capital	858,987	840,932
Accumulated other comprehensive income	1,424,274	577,574
Retained earnings	4,806,208	3,890,798
Treasury stock	(982,617)	(870,012)
Total shareholders' equity	6,231,421	4,566,861
Total liabilities and shareholders' equity	\$ 8,100,533	\$ 6,342,227

See Notes to Condensed Financial Statements and accompanying Report of Independent Registered Public Accounting Firm.

TORCHMARK CORPORATION
(PARENT COMPANY)
SCHEDULE II. CONDENSED FINANCIAL INFORMATION OF REGISTRANT (continued)
CONDENSED STATEMENTS OF OPERATIONS
(Dollar amounts in thousands)

	Year Ended December 31,		
	2017	2016	2015
Net investment income	\$ 26,130	\$ 25,352	\$ 23,715
Realized investment gains (losses)	(2,791)	—	8
Total revenue	<u>23,339</u>	<u>25,352</u>	<u>23,723</u>
General operating expenses	61,447	52,613	54,100
Reimbursements from affiliates	(52,776)	(54,288)	(53,436)
Interest expense	88,474	86,853	79,677
Total expenses	<u>97,145</u>	<u>85,178</u>	<u>80,341</u>
Operating income (loss) before income taxes and equity in earnings of affiliates	(73,806)	(59,826)	(56,618)
Income taxes	(9,874)	23,479	15,542
Net operating loss before equity in earnings of affiliates.....	(83,680)	(36,347)	(41,076)
Equity in earnings of affiliates	1,538,174	586,126	568,176
Net income	<u>1,454,494</u>	<u>549,779</u>	<u>527,100</u>
Other comprehensive income (loss):			
Attributable to Parent Company	(8,409)	(11,314)	(3,539)
Attributable to affiliates	602,709	356,941	(761,966)
Comprehensive income (loss)	<u>\$ 2,048,794</u>	<u>\$ 895,406</u>	<u>\$ (238,405)</u>

See Notes to Condensed Financial Statements and accompanying Report of Independent Registered Public Accounting Firm.

TORCHMARK CORPORATION
(PARENT COMPANY)
SCHEDULE II. CONDENSED FINANCIAL INFORMATION OF REGISTRANT—(continued)
CONDENSED STATEMENTS OF CASH FLOWS
(Dollar amounts in thousands)

	Year Ended December 31,		
	2017	2016	2015
Net income	\$ 1,454,494	\$ 549,779	\$ 527,100
Equity in earnings of affiliates	(1,538,174)	(586,126)	(568,176)
Cash dividends from subsidiaries	453,904	437,566	466,416
Other, net	52,957	(6,718)	20,371
Cash provided from operations	423,181	394,501	445,711
Cash provided from (used for) investing activities:			
Net decrease (increase) in short-term investments	(5,624)	(3,466)	17,338
Investment in subsidiaries	(31,000)	(35,000)	(2)
Additions to properties	(7,230)	(21,965)	(468)
Loaned money to affiliates	(180,000)	(363,056)	(282,508)
Repayments from affiliates	180,000	318,056	282,508
Cash provided from (used for) investing activities	(43,854)	(105,431)	16,868
Cash provided from (used for) financing activities:			
Repayment of debt	(126,875)	(250,000)	—
Proceeds from issuance of debt	125,000	400,000	—
Payment for debt issuance costs	(1,661)	(9,638)	—
Net issuance (repayment) of commercial paper	61,092	22,224	1,978
Issuance of stock	61,215	61,329	35,958
Acquisitions of treasury stock	(412,989)	(404,784)	(418,526)
Borrowed money from affiliate	278,500	60,000	15,000
Repayments to affiliates	(270,500)	(78,000)	(15,000)
Excess tax benefit on stock option exercises	—	—	8,180
Payment of dividends	(92,101)	(90,201)	(90,169)
Cash provided from (used for) financing activities	(378,319)	(289,070)	(462,579)
Net increase (decrease) in cash	1,008	—	—
Cash balance at beginning of period	—	—	—
Cash balance at end of period	<u>\$ 1,008</u>	<u>\$ —</u>	<u>\$ —</u>

See Notes to Condensed Financial Statements and accompanying Report of Independent Registered Public Accounting Firm.

TORCHMARK CORPORATION
(PARENT COMPANY)
SCHEDULE II. CONDENSED FINANCIAL INFORMATION OF REGISTRANT (continued)
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Dollar amounts in thousands)

Note A—Dividends from Subsidiaries

Cash dividends paid to Torchmark from the subsidiaries were as follows:

	Year Ended December 31,		
	2017	2016	2015
Dividends from subsidiaries	\$ 453,904	\$ 437,566	\$ 466,416

Note B—Supplemental Disclosures of Cash Flow Information

The following table summarizes noncash transactions, which are not reflected on the *Condensed Statements of Cash Flows*:

	Year Ended December 31,		
	2017	2016	2015
Stock-based compensation not involving cash	\$ 37,034	\$ 26,326	\$ 28,664
Borrowed money from affiliate	—	—	56,503
Investment in subsidiaries	317,027	—	39,206
Purchase of agent debit balances	—	—	17,297

The following table summarizes certain amounts paid (received) during the period:

	Year Ended December 31,		
	2017	2016	2015
Interest paid	\$ 86,606	\$ 84,952	\$ 77,920
Income taxes paid (received)	(19,961)	(20,838)	(22,009)

Note C—Preferred Stock

As of December 31, 2017, Torchmark had 351 thousand shares of Cumulative Preferred Stock, Series A, issued and outstanding, of which 280 thousand shares were 6.50% Cumulative Preferred Stock, Series A, and 71 thousand shares were 7.15% Cumulative Preferred Stock, Series A (collectively, the "Series A Preferred Stock"). All issued and outstanding shares of Series A Preferred Stock were held by wholly-owned insurance subsidiaries. In the event of liquidation, the holders of the Series A Preferred Stock at the time outstanding would be entitled to receive a liquidating distribution out of the assets legally available to stockholders in the amount of \$1 thousand per share or \$351 million in the aggregate, plus any accrued and unpaid dividends, before any distribution is made to holders of Torchmark common stock. Holders of Series A Preferred Stock do not have any voting rights nor have rights to convert such shares into shares of any other class of Torchmark capital stock.

See accompanying Report of Independent Registered Public Accounting Firm.

TORCHMARK CORPORATION
SCHEDULE IV. REINSURANCE (CONSOLIDATED)
(Dollar Amounts in thousands)

	<u>Gross Amount</u>	<u>Ceded to Other Companies⁽¹⁾</u>	<u>Assumed from Other Companies</u>	<u>Net Amount</u>	<u>Percentage of Amount Assumed to Net</u>
For the Year Ended December 31, 2017					
Life insurance in force	\$ 179,902,605	\$ 705,152	\$ 3,211,423	\$ 182,408,876	1.8
Premiums: ⁽²⁾					
Life insurance	\$ 2,272,038	\$ 4,437	\$ 21,912	\$ 2,289,513	1.0
Health insurance	980,082	3,709	—	976,373	—
Total premium	<u>\$ 3,252,120</u>	<u>\$ 8,146</u>	<u>\$ 21,912</u>	<u>\$ 3,265,886</u>	<u>0.7</u>
For the Year Ended December 31, 2016					
Life insurance in force	\$ 174,314,897	\$ 725,867	\$ 3,352,113	\$ 176,941,143	1.9
Premiums: ⁽²⁾					
Life insurance	\$ 2,152,698	\$ 4,507	\$ 22,915	\$ 2,171,106	1.1
Health insurance	951,137	3,474	—	947,663	—
Total premium	<u>\$ 3,103,835</u>	<u>\$ 7,981</u>	<u>\$ 22,915</u>	<u>\$ 3,118,769</u>	<u>0.7</u>
For the Year Ended December 31, 2015					
Life insurance in force	\$ 167,677,206	\$ 729,739	\$ 3,498,826	\$ 170,446,293	2.1
Premiums: ⁽²⁾					
Life insurance	\$ 2,034,373	\$ 4,484	\$ 24,007	\$ 2,053,896	1.2
Health insurance	928,659	3,139	—	925,520	—
Total premium	<u>\$ 2,963,032</u>	<u>\$ 7,623</u>	<u>\$ 24,007</u>	<u>\$ 2,979,416</u>	<u>0.8</u>

(1) No amounts have been netted against ceded premium.

(2) Excludes policy charges of \$17.0 million, \$18.3 million, and \$19.3 million in each of the years 2017, 2016, and 2015, respectively.

See accompanying Report of Independent Registered Public Accounting Firm.

Date: February 26, 2018

*By: /s/ FRANK M. SVOBODA
Frank M. Svoboda
Attorney-in-fact

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