



CONSOLIDATED FINANCIAL  
STATEMENTS

**In the right direction**

Consolidated Annual Report 2017



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## Independent auditors' report and consolidated financial statements for 2017

Quálitas Controladora, S.A.B. de C.V.  
and Subsidiaries

Consolidated financial statements  
December 31, 2017

## INDEPENDENT AUDITORS' REPORT

The Board of Directors and the Stockholders  
Quálitas Controladora, S. A. B. de C.V.:

[Figures in Mexican pesos]

Quálitas Controladora, S. A. B. de C. V. and subsidiaries  
Consolidated financial statements  
December 31, 2017 and 2016

[With Independent Auditors' Report Thereon]  
[Free Translation from Spanish Language Original]

### Opinion

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We have audited the consolidated financial statements of Quálitas Controladora, S. A. B. de C.V. and subsidiaries ("the Institution"), which comprise the consolidated balance sheets as at December 31, 2017 and 2016, statements of income, changes in stockholders' equity and cash flows for the years then ended, and notes, that include a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements of Quálitas Controladora, S. A. B. de C. V. and subsidiaries have been prepared, in all material respects, in accordance with Mexican Accounting Criteria for Insurance Institutions (the Accounting Criteria), issued by the National Insurance and Bonds Commission (the Commission).

### Basis for Opinion

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We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the consolidated Financial Statements section of our report. We are independent of the Institution in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Mexico, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Key Audit Matters

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The key audit matters are those that, in our professional judgment, have been most relevant in our audit of the consolidated financial statements of the current period. These matters have been addressed in the context of our audit of the overall consolidated financial statements and in forming our opinion thereupon we express no separate opinion on these matters.

**Technical reserves \$32,843,345,756**

See Note 3(m) to the consolidated financial statements..

The key audit matter	How the matter was addressed in our audit
<p>The valuation of technical reserves, depends on the quality of the underlying information. This translates in complexity and subjective judgement about future events, both internal and external, for which a change in assumptions, criteria or coverages may result in material impacts on estimates.</p>	<p>We were supported by our actuarial specialists to understand and evaluate the actuarial practices applied by the Institution in the calculation and in the accounting of the technical reserves, as well as consistency with the insurance regulation in force. We also consider, along with our actuarial specialists, the objectivity, competence, work and findings of independent actuaries engaged by Management, who assess the position and sufficiency of the technical reserves, including assessing assumptions and significant methods used by Management. Additionally, we evaluated that the information provided to the independent actuary was consistent with the information provided to us as part of our audit. Furthermore, we obtained an understanding of the process and tested the internal control implemented by the Institution for the creation of technical reserves, including the evaluation of the design and test of effectiveness of actuarial controls, which include reconciliations of key historical information and Management’s review of estimates. Additionally, because the historic information of the claims is relevant for estimates, we tested the controls and conducted substantive test of detail on the claims and payments thereof.</p>

**Other Information**

Management is responsible for the other information. The other information comprises information included in the Institution’s Annual Report corresponding to the year ended December 31, 2017, which is to be filed with the National Banking and Securities Commission (Comisión Nacional Bancaria y de Valores) and the Mexican Stock Exchange (the Annual Report), but do not include the consolidated financial statements and our auditors’ report thereon. It is estimated that the Annual Report will be available to us after the date of this auditors’ report.

Our opinion on the consolidated financial statements does not cover other information and we do not express any type of assurance conclusion thereon.

As for our audit of the consolidated financial statements, our responsibility is to read the other information, when available and, in doing so, consider if the other information is materially inconsistent with the consolidated financial statements or with our knowledge gained during the audit, or if it seems to be materially incorrect.

When we read the Annual Report, if we conclude that there is a material misstatement in such other information, we shall be required to report such fact to the persons responsible for the entity's governance.

### **Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements**

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Management is responsible for the preparation of the consolidated financial statements in accordance with the Accounting Criteria issued by the Commission, and for such internal control as Management deems necessary to enable the preparation of consolidated financial statements that are free of material misstatements, whether due to fraud or error.

In preparing the consolidated financial statements, Management is responsible for assessing the Institution's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management either intends to liquidate the Institution or to cease operations, or has no other realistic alternative.

Those charged with governance are responsible for overseeing the Institution's financial reporting process.

### **Auditors' Responsibilities for the Audit of the Consolidated Financial Statements**

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Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users made on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. Also:

- We identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures in response to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement due to fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- We obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Institution's internal control.
- We evaluate the appropriateness of accounting policies used and the reasonability of accounting estimates and related disclosures made by Management.
- We conclude on the appropriateness of Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant

doubt on the Institution's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Institution to cease to continue as a going concern.

- We obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Institution to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Institution audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify in the course of our audit.

We also provided those charged with the Institution's governance with a statement that we have complied with the ethics requirements applicable to independence and that we have communicated all relations and other matters reasonably expected to affect our independence and, where appropriate, the corresponding safeguards.

Among the matters that have been communicated to those charged with governance, we determine those that have been the most relevant in the audit of the financial statements of the current period and that are, consequently, key audit matters. We describe these matters in our audit report, unless the legal or regulatory provisions prohibit publicly disclosing the matter or, under extremely infrequent circumstances, we determine that a matter should not be communicated in our report because it is reasonable to expect that the adverse consequences of doing so would surpass the public interest benefits thereof.

**KPMG CARDENAS DOSAL, S. C.**



**C.P.C. Rafael Gutiérrez Lara**  
**Mexico City, February 16, 2018.**

## CONSOLIDATED BALANCE SHEET

December 31, 2017 and 2016 (Mexican pesos)

Assets	2017		2016	
Investment in securities (note 5):				
Government	\$ 11,371,416,494		4,505,048,223	
Corporate:				
Fixed income	8,566,640,973		8,917,133,890	
Variable income	4,106,985,405		3,949,293,679	
Foreign	347,654,422		711,456,313	
Impairment	(13,511,232)		-	
	24,379,186,062		18,082,932,105	
Repurchase agreements (note 5)	539,749,905		1,745,674,162	
Loan portfolio, net (note 6) :				
Current loan portfolio	374,437,585		406,536,256	
Past-due loan portfolio	30,343,004		19,699,081	
Allowance for loan losses	(3,392,422)		(3,398,356)	
	401,388,167		422,836,981	
Property, net (note 7)	1,414,605,750	26,734,929,884	1,323,912,491	21,575,355,739
Employee benefits investment (note 14)		59,827,988		68,405,674
Cash:				
Cash and cash in banks		746,632,032		753,995,698
Accounts receivable:				
Premiums (notes 8, 12 and 17)	18,213,615,893		14,996,166,140	
Receivables from agencies and public administration entities (notes 8 and 17)	131,553,979		42,527,919	
Agents and adjusters	134,814,171		109,756,972	
Notes receivables	4,695,000		4,695,000	
Other	880,279,595		689,922,882	
Allowance for doubtful accounts	(120,883,479)	19,244,075,159	(85,620,201)	15,757,448,712
Reinsurers:				
Current	4,322,290		2,782,263	
Recoverable reinsurance	86,125,830		116,141,324	
Credit risk allowance for foreign reinsurers	(1,733,933)		(1,311,275)	
Allowance for doubtful accounts	(29,706)	88,684,481	(96,739)	117,515,573
Permanent stock investments:				
Other permanent stock investments		48,364,995		50,174,320
Other assets (note 10):				
Furniture and equipment, net	824,290,745		599,924,094	
Other	3,228,074,147		2,268,277,686	
Amortizable intangible assets , net	84,401,039	4,136,765,931	41,723,751	2,909,925,531
<b>Total assets</b>	<b>\$</b>	<b>51,059,280,470</b>		<b>41,232,821,247</b>



<b>Liabilities and stockholders' equity</b>	<b>2017</b>		<b>2016</b>	
Liabilities:				
Technical reserves:				
Current risk:				
Property and casualty	\$ 24,106,291,723		20,119,047,953	
Outstanding claims provision:				
For expired policies and pending payment claims	8,049,950,518		6,104,325,437	
For claims incurred but not reported and adjustment expenses	72,276,161		35,126,316	
Advanced premiums	614,827,354		663,861,730	
	8,737,054,033	32,843,345,756	6,803,313,483	26,922,361,436
Employee benefits (note 14)		216,485,721		182,660,397
Creditors (note 11):				
Agents and adjusters	1,473,920,976		1,225,841,000	
Loss funds under management	5,618,558		6,390,501	
Sundry	3,198,862,532	4,678,402,066	2,815,674,528	4,047,906,029
Reinsurers (note 9):				
Current	48,793,218		93,477,624	
Retained deposits	15,910,013		-	
Other shares	2,664,353	67,367,584	-	93,477,624
Other liabilities:				
Employee statutory profit sharing (note 15)	368,132,732		217,720,251	
Income tax payable (note 15)	1,108,672,626		891,209,925	
Other	3,042,713,088		2,343,884,334	
Deferred credits	783,327,726	5,302,846,172	456,490,160	3,909,304,670
Total liabilities		43,108,447,299		35,155,710,156
Stockholders' equity (note 16):				
Controlling interest:				
Capital stock (note 16)		2,633,292,936		2,624,225,240
Reserve:				
Statutory	210,935,306		146,406,366	
Other	138,569,579	349,504,885	97,117,776	243,524,142
Valuation surplus		162,632,242		99,801,279
Retained earnings		2,518,628,729		1,562,624,403
Net income		2,056,233,236		1,290,578,806
Currency translation adjustment		184,042,491		217,390,325
Total controlling interest:		7,904,334,519		6,038,144,195
Non-controlling interest (note 19)		46,498,652		38,966,896
Total stockholders' equity		7,950,833,171		6,077,111,091
Commitments and contingencies (note 20)				
Total liabilities and stockholders' equity	\$	51,059,280,470		41,232,821,247

**Memorandum accounts**

Control accounts	\$	4,157,042,143	4,169,611,871
Funds under management		5,618,558	6,390,501
Collateral received from repurchase agreements		539,749,905	1,745,674,162

See accompanying notes to consolidated financial statements.

"Paid-in capital includes the amount of \$11,545,094 Mexican pesos, coming from the partial capitalization of real state valuation surplus."

"The consolidated balance sheets were prepared in accordance with the accounting provisions issued by the National Insurance and Bonds Commission (Comisión Nacional de Seguros y Fianzas), applied on a consistent basis, and taken as a whole, correctly reflect transactions performed by Quálitás Controladora, S. A. B. de C. V. and subsidiaries up to the aforementioned dates, which were carried out and valued in accordance with sound corporate practices and applicable legal and administrative provisions."

"The consolidated balance sheets were approved by the Board of Directors under the responsibility of the signing officers."

"The consolidated financial statements and the notes which form part of the consolidated financial statement can be consulted by Internet on the following webpage: <http://qinversionistas.Quálitás.com.mx/portal/documentos-regulatorios-q-mx>.

"The consolidated financial statements were audited by C.P.C. Rafael Gutiérrez Lara, a member of KPMG Cárdenas Dosal, S. C., who was hired to render the external auditing services to Quálitás Controladora, S. A. B. de C. V. and subsidiaries; furthermore, the technical reserves of Quálitás Controladora, S. A. B. de C. V. were audited by Actuary Luis Hernandez Frago"

"The report issued by the external auditor, the consolidated financial statements and the notes which form part of the audited consolidated financial statement and the report on the solvency and financial condition, will be made available for consultation on the following webpage: <http://qinversionistas.Quálitás.com.mx/portal/wp-content/uploads/Estados-Financieros-Consolidados2016.pdf> as of the sixty calendar days following the closing of the year 2017."

"Also, the Report on the Solvency and Financial Condition, will be located for consultation by Internet on the following webpage : <http://qinversionistas.Quálitás.com.mx/portal/wp-content/uploads/Reporte-Solvencia-Condicion-Financiera-2018.pdf> as of the ninety calendar days following the closing of the year 2017."



Lic. Joaquín Brockman Lozano  
Executive President equivalent to Chief  
Executive Officer



C.P.C. Gabriel García Ruíz  
Internal Auditor



C.P. Juan Daniel Muñoz Juárez  
General Accountant

## CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31, 2017 and 2016 (Mexican pesos)

	2017	2016
Premiums:		
Written (notes 12 and 17) \$	33,819,940,707	30,189,526,472
Less ceded (notes 9 and 17)	215,952,678	103,153,046
Retained premiums	33,603,988,029	30,086,373,426
Less net increase in current risks reserve (note 17)	4,936,254,551	6,261,775,172
Earned retained premiums (note 17)	28,667,733,478	23,824,598,254
Less:		
Net acquisition cost:		
Agent commissions	2,190,917,148	1,793,428,327
Additional compensation to agents	435,961,223	329,752,324
Reinsurance ceded commission	(1,820,189)	(4,939,083)
Non-proportional reinsurance cost	56,842,099	103,875,447
Other	5,168,865,354	7,850,765,635
	5,034,488,565	7,256,605,580
Net cost of claims and other outstanding obligations:		
Claims and other outstanding obligations	19,183,573,927	14,710,247,823
Technical and gross profit	1,633,393,916	1,857,744,851
Net operating expenses:		
Administrative and operating	(163,549,425)	(130,681,562)
Salaries and fringe benefits	690,760,651	626,885,920
Depreciation and amortization	327,741,507	254,503,489
Operating profit	778,441,183	1,107,037,004
Comprehensive financial result:		
Investment in securities	978,849,168	657,211,824
On sale of investments	671,659,825	(69,238,596)
Investment securities valuation	(511,386,846)	145,460,425
Premium surcharges	326,603,507	197,873,405
Interests from loans	43,433,110	29,791,708
Credit risk reserves from foreign reinsurers	(422,658)	(3,398,356)
Credit risk reserves	6,841	(1,311,275)
Other	251,604,753	67,025,267
Foreign exchange result (note 4)	68,844,821	(197,242,984)
Profit before taxes	2,607,633,704	1,933,208,422
Income tax, net (note 15)	544,012,870	632,589,872
Consolidated net income	2,063,620,834	1,300,618,550
Non-controlling interest (note 19)	(7,387,598)	(10,039,744)
Controlling interest \$	2,056,233,236	1,290,578,806
Basic and diluted earnings per share (note 18) \$	4.6590	2.9009

See accompanying notes to consolidated financial statements.

"These consolidated statements of income were prepared in accordance with the accounting provisions issued by the National Insurance and Bonds Commission (Comisión Nacional de Seguros y Fianzas), applied on a consistent basis, and reflect all the revenues and expenses derived from the transactions performed by Quálitas Controladora, S. A. B. de C. V. and subsidiaries up to the aforementioned dates, which were carried out and valued in accordance with sound corporate practices and applicable legal and administrative provisions."

"These consolidated statements of income were approved by the Board of Directors under the responsibility of the signing officers."



Lic. Joaquín Brockman Lozano  
Executive President equivalent to Chief  
Executive Officer



C.P.C. Gabriel García Ruiz  
Internal Auditor



C.P. Juan Daniel Muñoz Juárez  
General Accountant

## CONSOLIDATED STATEMENTS OF CHANGE IN STOCKHOLDERS' EQUITY

Years ended December 31, 2017 and 2016 (Mexican pesos)

	Paid in Capital Stock		Equity Earned	
	Capital stock	Capital reserves	Retained earnings	
			From prior years	
Balances as of December 31, 2015	\$ 2,578,777,564	253,602,979	1,424,985,322	
<b>Items related to stockholders' decisions:</b>				
Transfer of prior year's net income	-	192,803,387	363,264,350	
Dividends to stockholder's (note 16(d))	-	-	(225,000,000)	
Repurchase of shares	(38,684,868)	(118,749,680)	-	
Reclassification of repurchased shares from prior years	84,132,544	(84,132,544)	-	
<b>Items related to the comprehensive income (note 16(c)):</b>				
Valuation from property, net	-	-	-	
Remesurement of employee benefits	-	-	-	
Net income for the year	-	-	-	
Other	-	-	(625,269)	
Balances as of December 31, 2016	2,624,225,240	243,524,142	1,562,624,403	
<b>Items related to stockholders' decisions:</b>				
Transfer of prior year's net income	-	64,528,940	1,226,049,866	
Dividends to stockholder's (note 16(d))	-	-	(270,000,000)	
Resale of own shares (note 16(a))	9,067,696	41,451,803	-	
<b>Items related to the comprehensive income (note 16(c)):</b>				
Valuation from property, net	-	-	-	
Valuation from investment, net	-	-	-	
Remesurement of employee benefits	-	-	-	
Net income for the year	-	-	-	
Other	-	-	(45,540)	
Balances as of December 31, 2017	\$ 2,633,292,936	349,504,885	2,518,628,729	

See accompanying notes to consolidated financial statements.

"These consolidated statements of changes in stockholders' equity were prepared in accordance with the accounting provisions issued by the National Insurance and Bonds Commission (Comisión Nacional de Seguros y Fianzas), applied on a consistent basis, and reflect all the movements in the stockholders' equity accounts derived from the transactions performed by Quálitas Controladora, S. A. B. de C. V. and subsidiaries up to the aforementioned dates, which were carried out and valued in accordance with sound corporate practices and applicable legal and administrative provisions."

"These consolidated statements of changes in stockholders' equity were approved by the Board of Directors under the responsibility of the signing officers."

**Equity Earned**

Current year	Surplus from investment valuation	Currency translation adjustment	Total controlling interest	Non-controlling interest	Total stockholders equity
556,067,737	17,921,050	113,588,858	4,944,943,510	27,428,405	4,972,371,915
(556,067,737)	-	-	-	-	-
-	-	-	(225,000,000)	-	(225,000,000)
-	-	-	(157,434,548)	-	(157,434,548)
-	-	-	-	-	-
-	70,126,461	-	70,126,461	-	70,126,461
-	11,753,768	-	11,753,768	-	11,753,768
1,290,578,806	-	-	1,290,578,806	10,039,744	1,300,618,550
-	-	103,801,467	103,176,198	1,498,747	104,674,945
1,290,578,806	99,801,279	217,390,325	6,038,144,195	38,966,896	6,077,111,091
(1,290,578,806)	-	-	-	-	-
-	-	-	(270,000,000)	-	(270,000,000)
-	-	-	50,519,499	-	50,519,499
-	78,846,549	-	78,846,549	-	78,846,549
-	(11,875,146)	-	(11,875,146)	-	(11,875,146)
-	(4,140,440)	-	(4,140,440)	-	(4,140,440)
2,056,233,236	-	-	2,056,233,236	7,387,598	2,063,620,834
-	-	(33,347,834)	(33,393,374)	144,158	(33,249,216)
2,056,233,236	162,632,242	184,042,491	7,904,334,519	46,498,652	7,950,833,171



Lic. Joaquín Brockman Lozano  
Executive President equivalent to Chief  
Executive Officer



C.P.C. Gabriel García Ruíz  
Internal Auditor



C.P. Juan Daniel Muñoz Juárez  
General Accountant

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2017 and 2016 (Mexican pesos)

	2017	2016
Consolidated net income	\$ 2,063,620,834	1,300,618,550
Items not requiring cash:		
Gain on securities valuation	511,386,846	(145,460,425)
Depreciation and amortization	327,741,507	254,503,489
Adjustment or increase in technical reserves	4,936,254,551	5,857,165,340
Employee statutory profit sharing, net	217,823,519	213,007,958
Accruals	78,013,168	-
Allowance for loan losses	(5,934)	3,398,356
Allowance for doubtful accounts	35,263,278	(3,459,686)
Credit risk allowance on foreign reinsurers	422,658	1,311,275
Allowance for doubtful accounts on reinsurers	(67,033)	96,739
Current and deferred income tax	544,012,870	632,589,872
Subtotal	8,714,466,264	8,113,771,468
Operating activities:		
Changes in securities investment	(5,613,591,692)	(5,314,296,818)
Changes in loan portfolio	21,454,748	(192,982,319)
Changes in employee benefits, net	(34,675,045)	22,034,791
Changes in premiums receivable	(3,306,475,813)	(4,861,802,015)
Changes in other accounts receivable	(215,413,912)	(157,587,811)
Changes in reinsurers, net	2,365,427	56,084,195
Changes in other operating assets	(219,710,678)	(531,218,656)
Changes in obligations and expenses assigned to claims	984,729,769	2,307,965,344
Changes in sundry creditors	630,594,656	1,049,225,746
Changes in other operating liabilities	(133,200,175)	516,826,125
Net cash provided by operating activities	830,543,549	1,008,020,050
Investment activities:		
Sale (acquisition) of property	1,765,223	(197,348,529)
Acquisition of furniture and equipment	(453,139,135)	(193,252,953)
Acquisition of intangible assets	(135,514,293)	(6,442,764)
Disposal of other permanent investments	1,809,325	(2,482,255)
Net cash used in investing activities	(585,078,880)	(399,526,501)
Financing activities:		
Resale of own shares (repurchase of shares)	50,519,499	(157,434,548)
Dividends paid to stockholders	(270,000,000)	(225,000,000)
Net cash used in financing activities	(219,480,501)	(382,434,548)
Net increase in cash and cash equivalents	25,984,168	226,059,001
Effects of exchange rate and levels of inflation	(33,347,834)	103,801,467
Cash and cash equivalents:		
At beginning of year	753,995,698	424,135,230
At end of year	\$ 746,632,032	753,995,698

See accompanying notes to consolidated financial statements.

\*These consolidated statements of cash flows were prepared in accordance with the accounting provisions issued by the National Insurance and Bonds Commission (Comisión Nacional de Seguros y Fianzas), applied on a consistent basis, and reflect all the cash flows derived from the transactions performed by Quálitas Controladora, S. A. B. de C. V. and subsidiaries up to the aforementioned dates, which were carried out and valued in accordance with sound corporate practices and applicable legal and administrative provisions. \*

\*These consolidated statements of cash flows were approved by the Board of Directors under the responsibility of the signing officers.\*



Lic. Joaquín Brockman Lozano  
Executive President equivalent to Chief  
Executive Officer



C.P.C. Gabriel García Ruiz  
Internal Auditor



C.P. Juan Daniel Muñoz Juárez  
General Accountant

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 2017 and 2016 [Mexican pesos]

### (1) Description of business and credit rating-

#### Description of business

Quálitas Controladora, S. A. B. de C. V. [Quálitas Controladora and jointly with its subsidiaries, the Institution] is an institution incorporated under Mexican laws located at José María Castorena No. 426 Col. San José de los Cedros, Cuajimalpa de Morelos, Mexico City, C.P. 05200, Mexico.

The consolidated financial statements for the years ended December 31, 2017 and 2016 include those of Quálitas Controladora, S. A. B. de C. V. and subsidiaries. Quálitas Controladora through its main subsidiaries, is engaged in insurance, coinsurance and reinsurance as a property and liability insurer, specifically in the automobile line in terms of the Insurance and Bonds Institutions Law (the Law or LISF from its Spanish acronym).

The Institution conducts operations mainly in Mexico, United States of America, El Salvador and Costa Rica.

The main activities of the subsidiary companies are described below:

#### (a) Quálitas Compañía de Seguros, S. A. de C. V. [Quálitas Mexico]-

The principal activity of Quálitas Mexico is to engage, as laid down by Law, in insurance, coinsurance and reinsurance as a property and liability insurer in the automobile line; it is a 99.99% subsidiary of Quálitas Controladora and was incorporated on December 1, 1993 with a capital stock of \$7,500,000, which was paid up on the same date. Quálitas Mexico is the holding of Quálitas Compañía de Seguros, S. A. [Quálitas El Salvador] of which it owns 99.99% of its share capital. Quálitas El Salvador is primarily engaged in insurance, coinsurance and reinsurance as a property and liability insurer in the automobile line in terms of the Insurance Companies Law and its Regulations, the Commerce Code issued by the Legislature of El Salvador as well as of technical standards, administrative rules, regulations, bulletins and provisions issued by the Financial System Superintendence of such country.

#### (b) Quálitas Compañía de Seguros, S. A. [Quálitas Costa Rica]-

Quálitas Costa Rica is chiefly engaged in insurance, coinsurance and reinsurance as a property and liability insurer in the automobile line in terms of the Law issued by the Legislature of the Insurance Market No.8653 and the Commerce Code Law No.3284 issued by the Legislature of Costa Rica as well as of technical standards, administrative rules, regulations, bulletins and provisions issued by the General Insurance Superintendence of such country; it is a 99.99% subsidiary of Quálitas Controladora and was incorporated on February 28, 2011, with a capital stock of \$54,477,883, which was paid up on the same date.

#### (c) Quálitas Financial Services, Inc [Quálitas Financial]-

Quálitas Financial is primarily engaged in the incorporation, organization and management of business corporations in the United States of America; it is a 100% subsidiary of Quálitas Controladora and was incorporated on August 1, 2013 with a capital stock of \$196,264,500, paid up on the same date. Quálitas Financial is the 100% holding of Quálitas Insurance Company, Inc. [Quálitas Insurance], which main activity is insurance, coinsurance and reinsurance as a property and liability

insurer in the automobile line of insurance in terms of the California Department of Insurance, also Quálitas Financial is 100% holding company of Quálitas Premier Insurance Services (Quálitas Insurance Services), its primarily engaged is the services management.

### Credit rating

As of December 31, 2017 and 2016, the Institution and its subsidiaries have a credit rating for both years as follows:

Entity	Rating	Rating Agency
Quálitas Controladora	"BB+"	Standard & Poor's
Quálitas México	"mxA++"	Standard & Poor's
Quálitas Costa Rica	"BBB"	Pacific Credit Rating
Quálitas Financial	"BBB-"	Standard & Poor's

## (2) Authorization, basis of presentation and oversight-

### Authorization

On February 16, 2018, the Lic. Joaquín Brockman Lozano, Executive President equivalent to Chief Executive Officer authorized the issuance of accompanying consolidated financial statements and related notes thereto.

In accordance with the General Corporations Law, the provisions of the National Insurance and Bonds Commission (the Commission), and the bylaws of Quálitas Controladora, S. A.B. de C. V., the stockholders, the board of directors and the National Banking and Securities Commission (Comisión Nacional Bancaria y de Valores) are empowered to modify the consolidated financial statements after issued. The consolidated financial statements will be submitted to the next Stockholders' Meeting for approval.

### Basis of preparation

#### a) Statement of compliance

The accompanying consolidated financial statements have been prepared in accordance with Mexican accounting criteria for insurance institutions established by the Commission, in force as of the balance sheet date.

#### b) Use of estimates and judgments

The preparation of the financial statements requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include valuation of property, furniture and equipment, intangible assets; allowances for premiums receivable, loan portfolio, notes receivables, others notes receivables and valuation of deferred income tax assets and deferred employee statutory profit sharing; valuation of financial instruments, assets and liabilities related to employee benefits and technical reserves. Actual results could differ from those estimates and assumptions.



**c) Functional and reporting currency**

The aforementioned consolidated financial statements are presented in Mexican pesos (reporting currency), according to the following:

- For Quálitas Controladora and Quálitas Mexico the reporting currency is equal to the local currency and its functional currency.
- For Quálitas Costa Rica its local and functional currency is the colon and its financial statements were converted to Mexican peso, reporting currency, to present the consolidated financial statements.
- For Quálitas Financial its local and functional currency is the dollar and its financial statements were converted to Mexican peso, reporting currency, to present the consolidated financial statements.

For purposes of disclosure, “pesos” or “\$” means Mexican pesos, and “dollars” or “US\$” means U.S. dollars.

**Oversight**

The Commission is responsible for the inspection and oversight of insurance institutions and carries out a review of the annual consolidated financial statements and other periodic information which institutions are required to prepare.

**(3) Summary of significant accounting policies-**

The accounting policies set out in the next pages have been applied consistently to all these consolidated financial statements, and have been applied consistently by the Institution.

**(a) Inflation Effects Recognition-**

The accompanying consolidated financial statements have been prepared in accordance with the accounting criteria for Insurance companies in Mexico established by the Commission in effect as of the balance sheet date, and taking into account that the Institution operates in a non-inflationary economic environment it includes the recognition of the effects of inflation on the financial information through December 31, 2007 based on the Mexican National Consumer Price Index (NCPI). Annual and cumulative inflation percentages of the last three years and the indices used to determine inflation, are as follows:

December 31	INPC	Inflation	
		Yearly	Cumulative
2017	130.813	6.77%	12.71%
2016	122.515	3.36%	9.87%
2015	118.532	2.13%	10.52%

**(b) Principles of consolidation-**

The consolidated financial statements include the accounts of Quálitas Controladora, S. A. B. de C. V. and those of its subsidiaries which it controls. All significant inter-company balances and transactions have been eliminated in consolidation. The consolidation was based on the audited financial statements (except for Quálitas Financial) of the

issuing companies as of December 31, 2017 and 2016, which have been prepared in accordance with the accounting criteria for Insurance companies in Mexico established by the Commission and the Mexican Financial Reporting Standards (FRS) issued by the Mexican Board of Financial Reporting Standards (Consejo Mexicano de Normas de Información Financiera, A. C. or CINIF from its Spanish acronym) [See note 19].

**(c) Translation of foreign currency financial statements-**

The financial statements of foreign operations are translated into the reporting currency by initially determining if the functional currency and the currency for recording the foreign operations are different and then translating the functional currency to the reporting currency, using the historical exchange rate and/or the exchange rate at year end, and the inflation index of the country of origin when the foreign operation is located in an inflationary economy.

**(d) Investment in securities-**

The Commission regulates the basis on which the Institution makes investments, for which an accounting and valuation criteria has been established, which classifies the investments according to the management intention on ownership, as follows:

**Securities for trading purposes-**

Trading securities are debt or equity securities bought and held by the Institution to meet claims and operating expenses, so from the moment an investment is made there is an intention to trade them shortly, and in the case of debt securities on dates prior to maturity.

Debt securities are initially recorded at acquisition cost and performance accrual yield (interest, coupons or equivalents) is calculated by applying effective interest method. Interests are recorded on the income statement when earned. Traded debt securities are stated at fair value using market prices provided by independent price vendor, or by specialized official publications on international markets. When quotation is not available it could be used the acquisition cost as an indexed price for valuation.

Equity securities are recorded at acquisition cost and valued similarly to traded debt securities. Where there is no market value, the lower of the issuer's book value or acquisition cost shall be considered.

The valuation effects of debt and equity securities are recognized on the income statement in "Comprehensive financial results" under "Investment securities valuation".

On the date of its sale, the difference between the selling price and the carrying value of the securities will be recognized on the income statement. The sold securities' valuation result recognized on the income statement is reclassified to "Comprehensive financial result for the sale of investments" in the income statement, on the date of the sale.

At the acquisition date, transaction costs related to debt securities and equity are recorded on the income statement.

**Available-for-sale securities-**

These are those financial assets for which management has an intention other than an investment for trading purposes or to be held to maturity from the time of investment, and it is intended to trade them in the medium term and in the case of debt instruments on dates prior to maturity, in order to obtain gains based on the changes in market value and not only through inherent returns.

Debt securities are recorded at acquisition cost. Performance interest yield (interest, coupons or equivalents) and valuation methodologies are the same than those applied to trading debt securities, including yield earned on the income statement, however valuation effect is recorded on stockholders' equity under "Surplus from investments valuation" as long as such financial instruments are neither sold or transferred to a different category. At the time of sale, the effects previously recorded in equity, shall be recognized on the income statement

Equity instruments are recorded at acquisition cost. Investments in quoted shares are stated at fair value based on market prices released by independent price vendors, in the case where no market value is available, is considered the book value of the issuer. The valuation effects of equity instruments are recorded in the caption "Surplus from investment valuation" in stockholders' equity.

At the acquisition date, transaction costs related to debt securities and equity are recorded as part of the investment.

**Transfers between categories-**

Transfers between financial asset categories are permissible only when management's original intention for holding the financial asset is affected by changes in the Institution's financial capacity or a change in circumstances requiring modifying the original intent.

Only securities classified as available-for-sale may be transferred.

Transfer of categories of financial instruments for trading purposes is not allowed, except in case a financial instrument is in a market that, due to unusual circumstances outside the control of the Institution, ceases to be active and loses the characteristic of liquidity. This instrument may be transferred to financial instruments available-for-sale (debt or equity financial instruments).

**Unrealized valuation results-**

The Institution may not capitalize or share the profit from the valuation of any of the investments in securities until it is converted into cash.

**Repurchase operations-**

The repurchase operations are presented in a separate line item on the balance sheet. They are initially recorded at the agreed-upon price and valued at amortized cost, through the recognition of the premium in income of the year as accrued, following the effective interest method; financial assets received as collateral are recorded in memorandum accounts.

**Impairment-**

The Institution assesses at each balance sheet date whether there is objective evidence that a security is impaired, with the objective and non-temporary evidence that a financial instrument has impaired in value is determined and recognized a corresponding loss.

**(e) Cash and cash equivalents-**

Cash and cash equivalents include bank deposits in local currency and dollars. At the balance sheet date, interest earned and currency translation gains/losses are presented on the income statement as part of comprehensive financial result.

Checks that have not been charged after two business days after deposited, and those that have been returned, must be reclassified to sundry debtors. Forty-five days after the checks were recorded in sundry debtors and have not been collected or recovered should be written off affecting results from the operations of the year. Checks issued prior to date of the financial statements that have not been delivered to the beneficiaries, must be reclassified as a part of cash and cash equivalents without impacting the accounting records as a results of checks issuance.

**(f) Debtors-****Premiums receivable-**

Premiums receivable represents uncollected premiums with an aging lower than the term established in agreement or under 45-days aging according to the provisions of the Commission. When this status is exceeded, they are written off against the results of the year, except for premiums receivable from Federal Public Administration offices or entities, which are reclassified to "Receivables from agencies and public administration entities", if supported by a national public tender by these entities that signed, for purposes of the tender, and there is in place an agreement with the Federal Government supported in the Federal Expense Budget for the corresponding fiscal year.

**Loans to officers and employees, loans, credits or financing granted and other receivables-**

Management conducts an analysis on recoverability on loans to officers and employees, as well as on accounts receivable from identified debtors in which at inception maturity is agreed to be longer than a period of 90 calendar days, accounting for an allowance for doubtful accounts when needed.

In the case of accounts receivable not included in the preceding paragraph, an allowance for doubtful accounts is provided for the full amount, considering the following criteria: For unidentified debtors, right after 60 calendar days of being recorded, and in the case of identified debtors, right after 90 calendar days of being recorded.

The commercial loan portfolio is rated quarterly, monthly when it is comprised by mortgage loan, by applying a methodology that considers the probability of default, the severity of the loss and exposure to default, and recognizing the effect on the reserve in income of the year under "Comprehensive financing result".

The Commission may order the creation of preventive reserves from credit risk, in addition to those referred-to in the above paragraph, for the outstanding balance in the following cases:

- I. When the corresponding credits files have no or there is no documentation considered necessary according to the regulation in force, to exercise collection rights. This reserve is only released when the Institution addresses the deficiencies observed.
- II. When a report issued by a credit information company on the history of the borrower has not been obtained (except loans to officers and employees, when the loan payments are received through discounts to salary), this reserve is canceled three months after the required report is obtained.

**(g) Property, furniture and equipment-**

The Institution’s property is stated at acquisition cost and restated based on independent appraisals. Appraisals are required to be made annually.

Depreciation on property is calculated based on the remaining useful life of such assets, considering the restated value of constructions as determined by the latest appraisals performed.

Furniture and equipment are recorded at acquisition cost, and through December 31, 2007, were adjusted for inflation using the inflation index of the country of origin of the assets, and the variances in the exchange rate vis-à-vis the Mexican peso at year end.

Depreciation of furniture and equipment is calculated on the straight-line method over the estimated useful lives of the assets as determined by the Institution’s management. The annual depreciation rates of the principal asset classes are as follows:

	<b>Rates</b>
Property	1.25 to 4%
Transportation equipment	25%
Office furniture and equipment	10%
Computer equipment	30%
Other	25%

Leasehold improvements are amortized over the useful life of the improvement or the related contract term, whichever is shorter.

Minor repairs and maintenance costs are expensed as incurred.

**(h) Permanent Investments-**

The other permanent investments where the Institution holds between 1% and 16.67% of share in equity were carried at cost and, through December 31, 2007, adjusted for inflation by applying NCPI factors.

**(i) Goodwill-**

Goodwill represents the future financial benefits arising from other acquired assets that are not individually identifiable or separately recognizable. Goodwill is subject to impairment tests at the end of the reporting period and when there is an indication of impairment.

**(j) Intangible Assets-**

Intangible assets with definite useful life include mainly payments for the use of computer software licenses. The factors about the useful life are the expected use of the asset by the Institution and the typical life cycle of the software. These assets are recorded at acquisition cost and are amortized straight line over their estimated useful lives.

**(k) Prepayments-**

Mainly include prepayments for the purchase of services that are received after the date of the balance sheet and in the ordinary course of operations.

**(l) Other Assets-**

Other assets include mainly unrealized salvage inventory, prepayments, prepaid taxes, deferred income tax and deferred employee statutory profit sharing.

**(m) Technical reserves-**

The Institution constitutes and assesses the technical reserves established in the Law, in accordance with the general provisions issued by the Commission in Title 5 of the Provisions for Insurance and Bonds Institutions (the Provision or CUSF from its Spanish acronym).

The technical reserves are established and valued in relation to all insurance and reinsurance obligations that the Institution has assumed against the insured and beneficiaries of insurance and reinsurance contracts, the administration expenses, as well as the acquisition expenses assumed in relation thereto.

To establish and assess the technical reserves, actuarial methods based on the application of actuarial practice standards as dictated by the Commission through general provisions, will be used, and considering the information available in the financial markets, as well as the information available on technical insurance and reinsurance risks. The valuation of these reserves is assessed by an independent actuary and registered with the Commission.

For the technical reserves related catastrophic risk insurance and other reserves determined by the Commission according to the Law, the actuarial methods for establishment and valuation used by the Institution were determined by the Commission through general provisions.

The most important aspects to determine and account for the technical reserves are mentioned below.

### **Reserve for current risks-**

The institutions registered with the Commission the technical notes and the actuarial methods used for creating and valuing the current risk reserve.

The purpose of this reserve is cover the expected value of future obligations (best estimate), from the payment of claims, benefits, guaranteed securities, dividends, acquisition and administration expenses, as well as any other future obligation derived from the insurance contracts, plus a risk margin.

The best estimate will be equal to the expected value of the future flows, considering income and expenses, of obligations, understood as the weighted average by probability of these flows, considering the time value of money based on the curves of interest rate free of market risk for each currency or monetary unit provided by the independent price vendor, as of the valuation date. The hypothesis and procedures with which the future flows of obligations are determined, based on which the better estimate will be obtained, were defined by the Institution in the method submitted for the calculation of the best estimate.

For purposes of calculating the future flows of revenues, the premiums that upon valuation are past-due and outstanding are not considered, neither the fractional payments accounted for in "Premium receivable" in the balance sheet.

### **Multiannual insurance-**

In the case of multiannual policies, the current risk reserve is the best estimate of the future obligations of the current year, plus the rate premiums corresponding to future accumulated annuities with the corresponding return, for the time the policy has been in force, plus the risk margin. From premiums corresponding to future annuities the acquisition cost should be subtracted which for accounting purposes need to be recorded in a separate way to the reserve and upon writing insurance policy.

The Institution considers multiannual policies those insurance contracts whose coverage is more than one year, as long as it is not a long-term life insurance or insurance where the future premiums are contingent and it is not expected to be returned when the risk expires

### **Risk margin-**

This is calculated by determining the net cost of capital corresponding to the Own Admissible Funds required to support the Solvency Capital Requirement (RCS from its Spanish acronym), necessary to meet the Institution's insurance and reinsurance obligations over its duration. For purposes of valuation of the current risk reserve, the RCS of the month closing immediately preceding valuation date is used. If there are relevant increases or decreases in the amount of the Institution's obligations as of the report date, the Institution makes adjustments to this risk margin, which allows to recognize the increase or decrease the margin may have from the situations mentioned. In these cases, the Commission is informed of the adjustment made and the procedures used to make this adjustment.

The risk margin is determined for each type of insurance, taking into consideration term and currency considered in calculating the best estimate of the corresponding insurance obligation.

The net capital cost rate used to calculate the risk margin is 10%, equivalent to the additional interest rate, in relation

to the market risk free interest rate that an insurance institution would require to cover the capital cost demanded to maintain the amount of Own Admissible Funds supporting the respective RCS.

#### **Outstanding claims provision -**

The establishment, increase, valuation and recording of the reserve for outstanding obligations is made through estimating obligations using the actuarial methods the Institution has registered for such purposes with the Commission.

The purpose of this reserve is to cover the expected value of accidents, benefits, guaranteed values or dividends, once the contingency provided for in the insurance contract occurs, plus a risk margin.

The amount of the reserve for outstanding obligations will be equal to the sum of the best estimate and a risk margin, which are calculated separately and in terms of the provisions of Title 5 of the CUSF.

This reserve includes the following components:

#### *Outstanding claims provision and other known-amount obligations-*

- These are the outstanding obligations at closing of the period from claims reported, overdue endowments, past due income, guaranteed values and accrued dividends, among others, whose amount payable is determined upon valuation and is not likely to have adjustments in the future. The best estimate, for purposes of establishing this reserve is the amount corresponding to each one of the obligations known upon valuation.

For a future obligation payable in installments, the present value of future payment flows is estimated, discounted by applying the interest rate curves free of market risk for each currency or monetary unit, plus the risk margin calculated according to the provisions in force.

In case of reinsurance ceded operations, the corresponding recovery is recorded simultaneously.

#### *Reserve for claims incurred but not reported and adjustment expenses-*

- These are the obligations that arise from claims that having occurred as of the valuation date, have yet to be reported or have not been completely reported, as well as the adjustment, salvage and recovery expenses. The reserve upon valuation is determined as the best estimate of future obligations, brought to the present value using discount rates corresponding to the market risk free interest rate curves for each currency or monetary unit, plus the risk margin calculated according to the provisions in force. In case of reinsurance ceded operations, the corresponding recovery is recorded simultaneously. For purposes of calculating the reserve, a claim is defined as not having been completely reported when having occurred on dates prior to valuation of such claim, future claims or adjustments in addition to the estimates initially made, may derive.



### Risk margin-

This is calculated by determining the net capital cost corresponding to the Own Admissible Funds required to support the Solvency Capital Requirement (RCS), necessary to meet the insurance and reinsurance obligations over its duration. For purposes of valuation of the outstanding claims provision, the RCS of the month closing immediately preceding the valuation date is used. If there are relevant increase or decrease in the amount of the Institution's obligations as of the report date, the Institution makes adjustments to this risk margin, which allows to recognize the increase or decrease the margin may have from the situations mentioned. In these cases, the Commission is apprised of the adjustment made and the procedures used to make this adjustment.

The risk margin is determined for each type of insurance, taking into consideration term and currency considered in calculating the best estimate of the corresponding insurance obligation.

The net capital cost rate used to calculate the risk margin is 10%, equivalent to the additional interest rate, in relation to the market risk free interest rate that an insurance institution would require to cover the capital cost demanded to maintain the amount of Own Admissible Funds supporting the respective RCS.

### *Reserve for outstanding obligations from contingent dividends-*

This reserve corresponds to dividends that do not yet constitute actual or overdue obligations, but that the Institution estimates to pay in the future for the distribution obligations of the profits provided in the insurance contracts, from the favorable behavior of the risks, returns or expenses during the accrued duration period of the policies in force, the best estimate is determined by applying the method registered with the Commission. This methodology considers the repayment of a percentage of the premium collected through a dividend by claims, establishing the formula in its technical note for cars and vans of personal use up to 2 1/2 tons, which considers a return factor (assigned by volume of premiums) on the difference resulting from subtracting the total claims to the net premium earned less expenses.

### **(n) Accruals -**

Based on management estimates, the Institution recognizes accruals for present obligations where the transfer of assets or the rendering of services is virtually inevitable and arises as a consequence of past events, mainly acquisition costs, operating expenses and employee benefits.

### **(o) Employee benefits-**

#### **Short-term direct benefits**

Short-term direct employee benefits are recognized in income of the period in which the services rendered are accrued. A liability is recognized for the amount expected to be paid if the Institution has a legal or assumed obligation to pay this amount as a result of past services provided and the obligation can be reasonably estimated.

### Long-term direct benefits

The Institution's net obligation in relation to direct long-term benefits (except for deferred Employee Statutory Profit Sharing (ESPS) - see subsection (q) Income taxes and employee statutory profit sharing), and which the Institution is expected to pay at least twelve months after the date of the most recent balance sheet presented, is the amount of future benefits that employees have obtained in exchange for their service in the current and previous periods. This benefit is discounted to its present value. Remeasurements are recognized in income in the period in which they are accrued.

### Termination benefits

A liability is recognized for termination benefits along with a cost or expense when the Institution has no realistic alternative other than to make the corresponding payments or when the offer of these benefits cannot be withdrawn or when the conditions that require the recognition of restructuring costs are met, whichever occurs first.

### Post-Employment Benefits

#### *Defined benefit plans*

The Institution's net obligation in relation to defined benefit plans for pension, seniority premium and legal compensation benefits, is calculated separately for each plan, estimating the amount of future benefits that employees have earned in the current and prior periods, and discounting this amount to its present value.

The obligations for defined benefit plans are calculated annually by actuaries using the projected unit credit method. When the calculation results in a possible asset for the Institution, the recognized asset is limited to the present value of the economic benefits available in the form of future refunds of the plan or reductions in future contributions thereto. To calculate the present value of economic benefits, any minimum financing requirement should be considered.

The labor cost of current service, which represents the periodic cost of employee benefits for having completed one more year of working life based on the benefit plans, is recognized in operating expenses. The Institution determines the net interest income on the net defined benefit liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the net defined benefit liability, taking into account any changes in the net defined benefit liability during the period as a result of estimates of contributions and benefit payments. Net interest is recognized on the Consolidated Statement of income.

Modifications to the plans that affect past service cost are recognized in income immediately in the year the modification occurs, with no possibility of deferral in subsequent years. Furthermore, the effects of events of liquidation or reduction of obligations in the period that significantly reduce future service cost and/or significantly reduce the population eligible for benefits, are recognized in income of the period.

Remeasurements (formerly actuarial gains and losses), resulting from differences between the projected and actual actuarial assumptions at the end of the period, are recognized when incurred as part of comprehensive income within stockholder's equity.

**(p) Loss funds under management-**

It is related to the recorded amount of funds received for the payment of claims.

**(q) Income Tax and ESPS-**

IT and ESPS payable for the year are determined in conformity with the tax regulations in effect.

Deferred IT and ESPS are accounted for under the asset and liability method. Deferred taxes and ESPS assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and in the case of IT, for operating loss carryforwards and other recoverable tax credits. Deferred tax and ESPS 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 and ESPS assets and liabilities of a change in tax rates is recognized on the consolidated statement of comprehensive income in the period that includes the enactment date.

Current and deferred income taxes and ESPS are presented and classified in the results of operations of the period, except those arising from a transaction that is recognized directly in stockholders' equity.

**(r) Cumulative currency translation adjustment-**

Represent the difference resulting from the translation of the functional currency of foreign operations into the reporting currency.

**(s) Revenue recognition-****Insurance and reinsurance premium revenues -**

Revenues from these operations are recorded based on the premiums corresponding to the policies contracted, plus reinsurance premiums taken minus the premiums in reinsurance ceded.

The insurance premiums or the corresponding fraction, originated by the aforementioned operations that have not been paid by the insured within the term stipulated by the Law, are automatically canceled, releasing the current risk reserve and in the case of rehabilitation, the reserve is reconstituted as of the month in which the insurance is valid again.

**Salvage revenues-**

For accounting purposes, salvage revenues are recognized as an asset and a decrease in the cost of claims when determined, and are recorded at estimated realizable value.

**Profit sharing on reinsurance transactions-**

Profit sharing on reinsurance ceded is recorded as revenue based on the terms stipulated by the agreements included in the respective reinsurance contracts, as technical results thereof are determined.

**Policy rights and premium surcharges-**

Revenues related to policy rights are related to the recovery of costs of issuing the policy and are recorded on income statement as earned.

Revenues from premium surcharges is related to financing policies with periodic installments, which are deferred during policy term.

**Service revenues-**

The service revenues are recorded as earned.

**(t) Reinsurance-****Current account**

The transactions originated by the reinsurance contracts, both ceded and taken, issued by the Institution, are presented under "Current Account" in the balance sheet. For presentation purposes the net credit balances by reinsurer are reclassified to the corresponding liability.

**Reinsurance ceded**

The Institution limits the amount of its liability for risks assumed through the distribution with reinsurers, through automatic quota share and excess of loss contracts, transferring a portion of the premium to these reinsurers.

**Reinsurer's share in current risks and outstanding claims provision**

The Institution records the reinsurer's share in current risks and claims incurred but not reported and adjustment expenses, as well as the expected amount of future obligations from reported claims.

The Institution's management determines the estimate of the recoverable amounts for the share of reinsurers in the reserves mentioned in the above paragraph, considering the temporary difference between the reinsurance recovery and the direct payments and the probability of recovery, as well as the counterpart's expected losses. The calculation methodologies for this estimate are registered with the Commission, and the effect is recognized on the income statement under "Comprehensive financial result".

According to the provisions of the Commission, the recoverable amounts from reinsurance contracts with counterparts with no authorized registration, are not likely to cover the Investment Base, nor could they be part of the Own Admissible Funds (Fondos Propios Admisibles or FOPA for its Spanish acronym).

**(u) Net acquisition cost-**

This line item includes mainly the agent commissions that are recognized in income upon issuing the policies, additional compensation to agents and other acquisition expenses, and is decreased by the reinsurance ceded commission. The payment to agents is made when the premiums are collected.

**(v) Business concentration-**

The Institution performs transactions with a large number of clients, with no significant concentration with any of them in particular.

**(w) Comprehensive financial result (CFR)-**

The CFR includes interest income and expense, valuation effects, premium surcharges, results of selling financial instruments, foreign exchange gains and losses and preventive estimates of credit risk from loans granted and reinsurance amounts recoverable.

Transactions in foreign currencies are recorded at the exchange rate prevailing on the date of its execution or settlement. The Institution maintains its accounts in pesos and foreign currencies, which for purposes of presentation of financial statements were translated at the exchange rate of the last business day of the month, published by the Central Bank (see note 4). The exchange differences arising in relation to assets and liabilities denominated in foreign currencies are recorded in net income of the year.

**(x) Contingencies-**

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount thereof can be reasonably estimated. When a reasonable estimation cannot be made, qualitative disclosure is provided in the notes to the financial statements. Contingent revenues, earnings or assets are not recognized until their realization is assured.

**(y) Risk management-**

As part of the corporate governance system, the Institution has established the risk management system, which includes the definition and categorization of the risks the Institution might be exposed, taking in consideration, at least the following:

- I. Underwriting insurance risk- shows the risk arising from the underwriting, taking into account the claims covered and the operating processes linked to its management and, depending on the type of insurance, considers the premium and reserve risks, the expenses management, as well as extreme events.
- II. Market risk – shows the potential loss due to changes in risk factors that influence the value of assets and liabilities, such as interest rates, exchange rates, price indexes, among others.
- III. Mismatch between assets and liabilities risk - shows the potential loss resulting from the lack of structural correspondence between assets and liabilities, due to the fact that a position can not be covered by establishing an equivalent opposite position, and considers the duration, currency, interest rate, exchange rates, price indexes, among others.
- IV. Liquidity risk - shows the potential loss from the early or forced sale of assets at unusual discounts to meet obligations, or from the fact that a position can not be appropriately disposed of or acquired.
- V. Credit risk - shows the potential loss arising from non-collection, or impairment in the solvency of counterparties

and debtors in the operations carried out by the Institution, including the guarantees granted to it. This risk considers the potential loss arising from non-compliance with contracts intended to reduce risk, such as reinsurance contracts, as well as accounts receivable from intermediaries and other credit risks that can not be estimated with respect to the level of the risk-free interest rate.

- VI. Concentration risk - shows the potential losses associated with an inadequate diversification of assets and liabilities, and that is derived from exposures caused by credit, market, underwriting and liquidity risks, or by the combination or interaction of several of them, by counterpart, by type of asset, area of economic activity or geographical area.
- VII. Operational risk - shows the potential loss due to deficiencies or failures in the operating processes, in information technology, in human resources, or any other adverse external event related to the operation of the Institution such as legal risk, strategic risk and reputational risk, among others.

#### *Risk management policies*

The Board of Directors of the Institution has the general responsibility for the establishment and supervision of comprehensive risk management policies. The Board of Directors has implemented a comprehensive risk management system that is part of the organizational structure of the Institution, which is integrated to the decision-making processes and is supported by the internal control system designating a specific area of the Institution that is responsible of designing, implementing and monitoring the system of comprehensive risk management (Risk management area).

The institution's risk management policies are established to identify and analyze the risks faced by the Institution, establish adequate risk limits and controls, and monitor risks and compliance with limits. Risk management policies and systems are reviewed periodically to reflect changes in market conditions and the Institution's activities.

The purposes of the Risk Management Area are:

- I. Monitor, manage, measure, control, mitigate, and report on the risks to which the Institution is exposed, including those that are not perfectly quantifiable.
- II. Monitor that the performance of the Institution's operations is in accordance with the comprehensive risk management's limits, objectives, policies and procedures approved by the Board of Directors.

#### **[z] Hierarchy-**

Insurance institutions shall observe provisions under FRS, except when otherwise stated by the Commission, taking into consideration that insurance institutions conduct specialized operations.

In cases where insurance institutions consider that there is no accounting criterion applicable to any of the operation they carry out, issued by the Mexican Council of Financial Information Standards, A.C. (CINIF for its Spanish acronym) or the Commission, they will apply the hierarchy bases provided in NIF A-8, considering what is mentioned below:

- I. That in no case shall its application contravene the general concepts established in the accounting criteria for insurance institutions in Mexico established by the Commission
- II. That the rules that have been applied in the hierarchy process will be substituted, when a specific accounting criterion is issued by the Commission, or a FRS, on the subject in which said process was applied.

In case of following the hierarchy process, the Commission must be informed on the accounting standard that has been adopted, as well as its application base and the source used. In addition, the corresponding disclosures must be carried out in accordance with the regulations in force.

**(4) Foreign currency exposure-**

Monetary assets and liabilities denominated in dollars translated into the reporting currency, as of December 31, 2017 and 2016, were analyzed below:

		Mexican pesos	
		2017	2016
Assets	\$	3,258,770,750	2,597,127,074
Liabilities		(2,207,027,445)	(1,748,213,375)
Net assets	\$	1,051,743,305	848,913,699

As of December 31, 2017 and 2016 foreign exchange gain (losses) were recorded amounting to \$68,844,821 and (\$197,242,984), respectively.

The exchange rates used in the various translation processes to the reporting currency at December 31, 2017 and 2016 were as follows:

Country of origin	Currency	Year-end exchange rate		Average exchange rate	
		2017	2016	2017	2016
El Salvador	Dollars	19.6629	20.6194	18.8806	18.7193
United States of America	Dollars	19.6629	20.6194	18.8806	18.7193
Costa Rica	Colon	566.42	548.18	563.02	539.45

At December 31, 2017 and 2016, the Institution did not have foreign exchange hedging instruments.

**(5) Investments-**

At December 31, 2017 and 2016, the investment portfolio includes financial instruments held for trading purposes, which terms range between 4 days to 27 years and 3 days to 2 years, respectively.

At December 31, 2017 and 2016, interest rates applied to financial instruments held for trading purposes portfolio range between 1.18% to 11.45% and .01% to 8.15%, respectively.

	2017				2016			
	Amount	Accrued interest	Increase (decrease) in valuation	Total	Amount	Accrued interest	Increase (decrease) in valuation	Total
Debt securities:								
Government securities:								
For trading purposes								
BANOBRA	\$ 4,172,792,345	23,377	2,000,435	4,174,816,157	1,990,231,685	-	(14,716)	1,990,216,969
NAFIN	2,361,496,708	682,124	243,934	2,362,422,766	835,110,994	-	(2,557)	835,108,437
CETES	1,732,305,334	-	46,060,301	1,778,365,635	-	-	-	-
SHF	1,046,996,417	-	663,942	1,047,660,359	660,534,174	-	(2,022)	660,532,152
BONDESD	668,693,025	2,420,365	(1,809,196)	669,304,194	117,972,147	19,060	(44,849)	117,946,358
BPA	70,064,105	(405,016)	(405,016)	70,230,078	-	-	-	-
BNCEB56	15,455,787	227,914	119,263	15,802,964	-	-	-	-
NOTAS SV	11,290,437	-	-	11,290,437	11,671,901	167,758	-	11,839,659
US GOVERNMENT BONDS	1,156,509,808	-	5,387,295	1,161,897,103	866,980,667	-	22,423,981	889,404,648
	11,235,603,966	3,924,769	52,260,958	11,291,789,693	4,482,501,568	186,818	22,359,837	4,505,048,223
Available-for-sale securities								
US GOVERNMENT BONDS	89,297,375	-	(9,670,574)	79,626,801	-	-	-	-
	\$ 11,324,901,341	3,924,769	42,590,384	11,371,416,494	4,482,501,568	186,818	22,359,837	4,505,048,223
Private companies securities known rate:								
For trading purposes								
Financial sector	\$ 4,532,440,569	19,773,754	(28,265,066)	4,523,949,257	3,439,621,721	10,362,770	(3,035,758)	3,446,948,733
Non-financial sector	3,690,680,671	18,998,256	104,993,502	3,814,672,429	5,356,500,716	21,824,657	91,859,784	5,470,185,157
	8,223,121,240	38,772,010	76,728,436	8,338,621,686	8,796,122,437	32,187,427	88,824,026	8,917,133,890
Available-for-sale securities								
Non-financial sector	226,387,422	3,683,894	(2,052,029)	228,019,287	-	-	-	-
	\$ 8,449,508,662	42,455,904	74,676,407	8,566,640,973	8,796,122,437	32,187,427	88,824,026	8,917,133,890
Foreign securities:								
For trading purposes								
Investment in foreign securities	\$ 187,400,354	17,874	160,236,194	347,654,422	536,961,908	-	174,494,405	711,456,313
Equity securities:								
Private companies securities, variable income:								
For trading purposes								
Financial sector	\$ 165,562,511	-	53,558,111	219,120,622	33,156,750	-	11,618,750	44,775,500
Non-financial sector								
TAURUM B-M1	3,314,999,992	-	30,298,549	3,345,298,541	999,999,999	-	34,147,288	1,034,147,287
Other	360,739,363	-	181,826,879	542,566,242	2,135,245,884	-	735,125,008	2,870,370,892
	\$ 3,841,301,866	-	265,683,539	4,106,985,405	3,168,402,633	-	780,891,046	3,949,293,679
Total accrued interests		\$ 42,714,653				\$ 32,374,245		
Total valuation increase, net			\$ 545,238,553				\$ 1,066,569,314	



		2017	2016
Repurchase agreements:			
BONDES	\$	366,116,889	275,259,000
GANACB		53,440,810	-
FEFA		40,377,092	-
IQ210422		28,762,063	-
ABCCB		18,982,154	-
SHF 0001		10,720,018	-
SGMEX 16D		10,096,873	-
TFOVIS		5,633,359	-
CETES		4,317,343	8,650,338
BPA182		1,065,492	156,842,708
ELEKTRA		237,812	-
BONOS		-	508,796,154
BPAG28		-	242,424,861
SCOTIAB		-	3,919,681
UDIBONO		-	481,620,903
AERMxCB		-	1,339,017
CHIACB		-	62,320,497
BACOMER		-	4,501,003
	\$	539,749,905	1,745,674,162

At December 31, 2017 and 2016, financial instruments are analyzed as shown on the following page.

#### (6) Loan portfolio-

At December 31, 2017 and 2016, the current loan portfolio is comprised by the following:

		2017	2016
Mortgage	\$	10,630,973	4,477,510
Unsecured		73,081,032	108,499,480
Discount and rediscount		290,258,710	292,443,695
Accrued interest		466,870	1,115,571
	\$	374,437,585	406,536,256

At December 31, 2017 and 2016, the Institution in accumulate way has recognized \$30,343,004 and \$19,699,081 of past-due portfolio. Also \$3,392,422 and \$3,398,356, of allowance for loan losses, respectively were provided.

At December 31, 2017 and 2016, unsecured loans are analyzed as follows:

		2017	2016
Rosas Abarca y Asociados, S. C.	\$	11,500,000	8,000,000
Autofinanciamiento de Automóviles, S. A. de C. V.		9,322,151	15,000,000
Ibrahim Hakim Samy		4,832,533	-
Dynamic Network Insurance		2,088,133	-
Promotoría Virtual, S. A. de C. V.		-	5,222,598
Willis Agente de Seguros y de Fianzas, S. A. de C. V.		-	6,623,661
Bituaj, Agente de Seguros y de Fianzas, S. A. de C. V.		-	7,767,730
PVM Agente de Seguros, S. A. de C. V.		-	12,577,846
Other		45,338,215	53,307,645
	\$	73,081,032	108,499,480

At December 31, 2017 and 2016, discount and rediscount loans are analyzed as follows:

		2017	2016
Promotora Sku, S. A. P. I. de C. V. SOFOM E.N.R.	\$	146,230,950	115,999,273
Firma Car, S. A. P. I. de C. V.		72,666,649	55,569,422
GT Credit, S. A. P. I. de C. V. SOFOM E.N.R.		48,611,111	70,000,000
CI Banco, S.A. Institución de Banca Múltiple		18,750,000	46,875,000
Credicam, S. A. de C. V. SOFOM E.N.R.		4,000,000	4,000,000
	\$	290,258,710	292,443,695

## (7) Property-

At December 31, 2017 and 2016, property is analyzed as follows:

		2017	2016
Land	\$	374,999,744	382,789,594
Buildings		412,048,772	402,405,182
Special facilities		28,983,737	29,093,489
		816,032,253	814,288,265
Accumulated depreciation		(70,874,352)	(61,233,123)
		745,157,901	753,055,142
Net valuation		669,447,849	570,857,349
Total	\$	1,414,605,750	1,323,912,491

At December 31, 2017 and 2016, the Institution made appraisals of its properties, as a result an increase in their value of \$98,590,500 and \$118,091,278 was recorded, respectively. Depreciation is calculated based on the remaining useful life and the restated value of buildings, determined through the latest appraisals made. The applicable depreciation rate for 2017 ranges between 1.26% and 2.04% (1.25% and 4% rate for 2016).

**(8) Accounts receivable-**

**Premiums -**

At December 31, 2017 and 2016 premiums receivable are analyzed below:

	2017	2016
Automobile:		
Fleets, financial and other	\$ 14,038,739,531	9,414,806,716
Individual	3,838,217,542	5,176,915,807
Foreign	336,658,820	404,443,617
	18,213,615,893	14,996,166,140
Receivables from agencies and entities of the federal public administration	131,553,979	42,527,919
	\$ 18,345,169,872	15,038,694,059

At December 31, 2017 and 2016 premiums receivable accounts represent 36% of total assets in both years.

**(9) Reinsurers-**

At December 31, 2017 and 2016, balances receivable from reinsurers is analyzed as follows:

Institution	2017		
	Up to 90 days	More than 180 and up to 365 days	Total
Kot Insurance Company, A.G.	\$ -	7,977,653	7,977,653
Financial Insurance Company Limited	-	12,520,080	12,520,080
Other	-	28,295,485	28,295,485
Total	\$ -	48,793,218	48,793,218
Percentage	0%	100%	100%

Institution	2016		
	Up to 90 days	More than 180 and up to 365 days	Total
Kot Insurance Company, A.G.	\$ -	64,204,855	64,204,855
Paramount General Agency, Inc	-	6,004,382	6,004,382
Sun Coast General Insurance Agency, Inc	-	7,351,672	7,351,672
First Capital - Awis LLC	3,231,667	-	3,231,667
Other	1,213,628	11,471,420	12,685,048
Total	\$ 4,445,295	89,032,329	93,477,624
Percentage	5%	95%	100%

At December 31, 2017 and 2016, the Institution ceded premiums in the property and casualty (automobile insurance) were \$215,952,678 and \$103,153,046, respectively.

**[10] Other assets-**

Furniture and equipment:

At December 31, 2017 and 2016 furniture and equipment are as shown on the next page.

	2017	2016	Annual depreciation rate
Office furniture and equipment	276,993,518	261,158,076	10%
Computer equipment	\$ 838,410,369	639,692,723	30%
Transportation equipment	471,531,300	401,917,700	25%
Other	568,810,337	388,452,544	25%
	2,155,745,524	1,691,221,043	
Less accumulated depreciation	1,331,454,779	1,091,296,949	
	\$ 824,290,745	599,924,094	

Other:

At December 31, 2017 and 2016 this caption is analyzed as follows:

	2017	2016
Unrealized salvage inventory	\$ 549,144,209	541,314,807
Spare parts inventory	80,793,220	81,394,897
Prepayments	283,294,283	393,594,318
Income tax prepayments	945,932,889	630,890,171
Deferred income tax (note 15)	1,056,098,194	477,059,527
Deferred employee statutory profit sharing (note 15)	312,811,352	144,023,966
	\$ 3,228,074,147	2,268,277,686

At December 31, 2017 and 2016, the "Amortizable intangible assets" includes mainly computer software licenses, amortized at the rate of 33.33%.

**[11] Creditors-**

At December 31, 2017 and 2016 creditors are as follows:

	2017	2016
Use of facilities	\$ 2,383,674,600	2,140,051,558
Agents	1,473,920,976	1,225,841,000
Other	410,025,542	477,813,921
Amounts withheld from adjusters	115,027,138	103,843,086
Accruals	290,135,252	93,965,963
Loss funds under management	5,618,558	6,390,501
	\$ 4,678,402,066	4,047,906,029

**[12] Written premiums and issued in advance to the risk period covered -**
**Written premiums**

The value of written premiums by the Institution as for the years ended December 31, 2017 and 2016 are analyzed below:

	2017	2016
Automobile:		
Fleets, financial and other	25,240,143,658	24,309,873,258
Individual	6,900,702,298	4,426,624,511
Foreign	1,679,094,751	1,453,028,703
	\$ 33,819,940,707	30,189,526,472

**Premiums issued in advance to the risk period covered**

At the years end 2017 and 2016, the Institution issued premiums, which period covered starts in years 2018 and 2017, respectively. Following are the transactions related to premiums issued in advance to the risk period covered:

	2017	2016
Premiums issued in advance to the risk period covered:		
Issued	\$ 3,028,422,273	2,771,516,369
Ceded	23,200	376,287
Increase in currents risks reserve	\$ 2,415,603,647	2,107,950,805
Agent commissions	108,539,456	65,636,569
Policy rights	100,658,905	85,272,446
Acquisition cost	619,200,605	643,367,770

At December 31, 2017 and 2016 the amounts related to premiums issued in advance to the risk period covered are analyzed below:

	2017	2016
Premiums receivable	\$ 3,703,231,234	3,339,226,942
Reinsurers current account	23,220	376,287
Currents risks reserve	2,415,603,647	2,107,950,805
Premium surcharges	63,359,541	21,870,411
Value added tax to be accrued	510,790,515	460,567,716
Commissions to be accrued	108,539,456	65,636,569
Creditors (Use of facilities)	619,200,605	643,367,770

**(13) Basis of Investment, RCS and minimum paid in capital-**

Quálitas México is subject to the following liquidity and solvency requirements:

Basis of Investment - It is the sum of the technical reserves, advanced premiums and funds related to policy dividends management.

RCS - It is determined in accordance with the requirements established in the Law and in accordance with the general formula established in the provisions issued by the Commission. The purpose of this requirement is:

- I. To have sufficient patrimonial resources in relation to the risks and responsibilities assumed by the Institution in function of its operations and, in general, of the different risks to which it is exposed;
- II. The development of adequate policies for the selection and underwriting of insurance, as well as for the dispersion of risks with reinsurers in the transfer and acceptance of reinsurance operations;
- III. To have an appropriate level of patrimonial resources, in relation to the financial risks that the Institution assumes, when investing the resources obtained from its operations, and
- IV. The determination of the assumptions and patrimonial resources that the Institution must maintain in order to deal with situations of an exceptional nature that put its solvency or stability at risk, derived both from the particular operation and from market conditions.

Minimum paid-in capital - It is a capital requirement that must be met by the Institution for each operation or line that is authorized (see note 16b).

In the next page presents the coverage of the aforementioned requirements.

Statutory Requirements	Coverage of statutory requirements			
	Surplus (Deficit)		Coverage Index	
	Current year	Prior year	Current year	Prior year
Technical reserves <sup>1</sup>	3,097,214,670	818,050,986	1.10	1.03
Solvency capital requirement <sup>2</sup>	2,658,935,790	946,029,787	1.90	1.35
Minimum capital requirement <sup>3</sup>	5,805,185,576	4,047,968,674	123.47	89.28

<sup>1</sup> Investments that support technical reserves / basis of investment.

<sup>2</sup> FOPA / RCS.

<sup>3</sup> The Institution's capital resources computable according to the regulation / Requirement of minimum paid-in capital for each operation and / or line that is authorized.

**(14) Employee benefits-**

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The Institution has a defined benefit pension plan covering employees aged 65 or 60 provided they have 10 or more years of services and reducing 3% of the pension each year in which individual anticipate the normal retirement age, which consists of granting the pensionable salary, which is comprised by the average salary for the plan's purposes over the last 12 months prior to the retirement date, including the year-end bonus, divided by twelve and excluding all other compensation in cash or in kind.

This plan also covers seniority premiums, which are a single payment equivalent to 12 days for each year worked and considering the last salary received and limited to two times the minimum daily wage established by law.

Moreover, this plan also covers termination benefits, which consist of a single payment of three months of integrated salary, plus 20 days for each year worked, based on the last salary earned by the employee.

The related liability and the annual benefit cost are calculated by an independent actuary in accordance with the plan rules, using the projected unit credit method.

**a) Short-term direct benefits-**

These correspond to cumulative accrued remunerations granted and paid regularly to the employee, such as salaries, vacations, vacation premium and compensations.

**b) Post-employment benefits-**

Currently, the Institution recognizes benefits (seniority premiums and statutory severance pay) as required by the pensions plan, which covers all plant and full-time employees. This benefit consists of providing a pension in addition to the pension granted by the Mexican Institute of Social Security, according to the years of service at the Institution. The regular retirement pension shall be a joint lifelong monthly annuity, with a guarantee of 240 payments. These payments shall be paid in arrears and be equivalent to: 0.33% of the pensionable salary for each pensionable year of service, increased by 4.5 years.

There were no contributions and benefits paid from the funds in 2017 and 2016.

The cost components of defined benefits for the year ended December 31, 2017 and 2016 are analyzed bellow:



	Seniority premium		Legal compensation		Pension plan	
	2017	2016	2017	2016	2017	2016
Current Service Cost (CLSA)	\$ 2,600,061	2,552,656	33,082,626	8,872,987	33,412,617	13,578,226
Net interest on Defined Benefits Net Liability (DBNL)	390,663	360,407	3,333,880	2,702,909	4,659,647	3,840,167
Reclassification of remeasurements of DBNL recognized in comprehensive income	(66,125)	22,444	1,478,024	2,255,206	(878,225)	(537,980)
Reduction effect	-	-	-	23,658,968	-	-
<b>Defined Benefit Cost</b>	\$ 2,924,599	2,935,507	37,894,530	37,490,070	37,194,039	16,880,413
Beginning balance of DBNL remeasurements	\$ (934,576)	317,212	8,918,221	13,612,084	(19,737,413)	(12,044,990)
Remeasurements generated in the year	66,125	(1,229,344)	(1,478,024)	(2,438,657)	878,225	(8,230,403)
Reclassification of remeasurements recognized in comprehensive income in the year	1,251,497	(22,444)	(1,283,192)	(2,255,206)	(369,745)	537,980
<b>Ending balance of DBNL remeasurements</b>	\$ 383,046	(934,576)	6,157,005	8,918,221	(19,228,933)	(19,737,413)
Beginning balance of DBNL	\$ 4,883,286	4,971,133	51,125,854	47,800,343	58,245,583	51,202,224
Defined benefit cost	2,924,599	2,935,507	37,894,530	37,490,070	37,194,039	16,880,413
Payments charged to DBNL	(1,728,953)	(1,771,566)	(29,754,065)	(29,470,696)	(3,192,026)	(2,144,631)
Effect in comprehensive income	1,317,622	(1,251,788)	(2,761,216)	(4,693,863)	508,480	(7,692,423)
<b>Ending balance of DBNL</b>	\$ 7,396,554	4,883,286	56,505,103	51,125,854	92,756,076	58,245,583
Defined benefit obligations (OBD)	\$ 18,364,109	15,340,606	56,505,103	51,125,854	140,925,447	116,193,937
Plan assets	(10,967,555)	(10,457,320)	-	-	(48,169,371)	(57,948,354)
<b>Financial position of the obligation</b>	\$ 7,396,554	4,883,286	56,505,103	51,125,854	92,756,076	58,245,583

	2017	2016
Nominal discount rate used in calculating the present value of obligations:		
Seniority premium	7.75%	8.00%
Legal compensation	7.50%	7.25%
Pension plan	7.75%	8.00%
Expected rate of return on plan assets:		
Seniority premium	7.75%	8.00%
Legal compensation	7.75%	8.00%
Nominal increase rate for salaries	4.50%	4.50%
Average remaining service life of the Institution's employees:		
Seniority premium	14 years	14 years
Legal compensation	6 years	6 years
Pension plan	23 years	22 years

### (15) Income tax (IT) and employee statutory profit sharing (ESPS) -

IT Law effective as of January 1, 2014 imposes an IT rate of 30% for 2014 and thereafter.

#### a) Income tax

The income tax expense is as follows:

	2017	2016
On income statement:		
IT current	\$ 1,135,442,764	902,766,354
IT deferred	(591,429,894)	(270,176,482)
	\$ 544,012,870	632,589,872
On stockholders' equity – IT deferred	\$ 20,131,496	35,063,230

For the years ended December 31, 2017 and 2016, the IT on a current and deferred basis in the consolidated statement of income is shown below:

		2017	2016
<b>Current:</b>			
Quálitas México	\$	1,107,936,944	889,796,429
Quálitas Costa Rica		8,944,406	5,103,914
Quálitas Financial		-	489,884
Other subsidiaries		18,561,414	7,376,127
		1,135,442,764	902,766,354
<b>Deferred:</b>			
Quálitas México		(570,659,046)	(272,203,623)
Quálitas Costa Rica		(603,751)	(72,835)
Quálitas Financial		(18,582,292)	(8,309,366)
Other subsidiaries		(1,584,805)	10,409,342
		(591,429,894)	(270,176,482)
<b>Total</b>	<b>\$</b>	<b>544,012,870</b>	<b>632,589,872</b>

Income tax expense attributable to income from continuing operations before income taxes, differed from the amounts computed by applying the Mexican statutory rate of 30% IT to income before income taxes, as a result of the items shown below:

		2017	2016
Computed "expected" tax expense	\$	782,290,111	579,962,527
Add ESPS expense		(8,202,438)	33,203,832
<b>Increase (reduction) resulting from:</b>			
Accounting loss on sale of shares		(90,215,241)	20,844,915
Dividends		(8,697,653)	(28,691,339)
Tax effects of inflation, net		(30,526,423)	(13,080,858)
Non-deductible expenses		37,143,507	35,046,107
Other, net		(137,778,993)	5,304,688
<b>IT expense</b>	<b>\$</b>	<b>544,012,870</b>	<b>632,589,872</b>

The tax effects of temporary differences that give rise to significant portions of the deferred IT assets and liabilities, at December 31, 2017 and 2016, are as follows:

	2017	2016
Deferred assets:		
Premium surcharges	\$ 226,760,963	130,969,446
Commissions to be accrued	169,861,988	126,636,417
Additional compensation to agents	46,693,477	39,038,682
Use of facilities	715,102,380	642,015,467
ESPS payable	110,439,820	30,698,555
Employee benefits	22,088,740	16,109,916
Provisions	94,887,219	39,626,491
Tax loss carry forwards	11,314,086	17,144,601
Other	51,099,693	45,202,236
Total deferred assets	1,448,248,366	1,087,441,811
Deferred liabilities:		
Salvage inventory	(164,595,790)	(162,394,442)
Valuation from property	(149,363,527)	(165,247,157)
Valuation from investments	(164,687,575)	(313,523,280)
Other	86,496,720	30,782,595
Total deferred liabilities	(392,150,172)	(610,382,284)
Deferred tax assets, net	\$ 1,056,098,194	477,059,527

As of December 31, 2017 and 2016, the Institution has a liability for the payment of deferred income taxes of Activos Jal, which is generated by the valuation of the properties amounting to \$15,234,460 and \$9,532,878, respectively.

**b) ESPS and deferred ESPS**

The ESPS expense is as follows:

	2017	2016
On income statement:		
ESPS	391,298,913	305,876,585
Deferred ESPS	\$ (173,475,394)	(92,868,627)
	217,823,519	213,007,958
On stockholders' equity: - Deferred ESPS	\$ 4,688,008	11,687,743

The ESPS temporary differences that give rise to significant portions of the deferred ESPS assets and liabilities, at December 31, 2017 and 2016 are as follows:

	2017	2016
Deferred assets:		
Premium surcharges	\$ 75,586,988	43,656,482
Commissions to be accrued	56,620,663	42,212,138
Additional compensation to agents	15,564,492	13,012,893
Use of facilities	238,367,460	214,005,156
Employee benefits	15,665,773	6,055,500
Provisions	34,578,521	13,743,795
Other	7,144,180	9,923,175
Total deferred assets	443,528,077	342,609,139
Deferred liabilities:		
Salvage inventory	[54,865,264]	[54,131,481]
Valuation from property	[49,787,842]	[44,992,358]
Valuation from investments	[54,895,858]	[104,507,759]
Other	28,832,239	5,046,425
Total deferred liabilities	[130,716,725]	[198,585,173]
Deferred tax assets, net	\$ 312,811,352	144,023,966

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

## (16) Stockholder's equity-

The main characteristics of stockholders' equity are described below:

### (a) Structure of capital stock -

At December 31, 2017 and 2016, capital stock is represented by 450,000,000 common, registered single series (Series I) shares with an updated par value of \$5.9664 and a historical value of \$5.6913, which represent the fixed unlimited portion, which is duly subscribed and paid-in, 441,352,434 of which are shares outstanding (439,832,645 at December 31, 2016). During 2017, the Institution resold 1,519,789 of its own shares for \$9,067,696 which corresponds to their par value.

At December 31, 2017 and 2016, structure of capital stock is comprised of the following:

	Nominal	Revaluation	Total
Capital stock	\$ 2,512,284,861	121,008,075	2,633,292,936
Statutory reserve	339,731,240	9,773,645	349,504,885
Valuation surplus, net	-	162,632,242	162,632,242
Foreign currency translation adjustment on foreign operations	184,042,491	-	184,042,491
Retained earnings	2,612,617,675	[93,988,946]	2,518,628,729
Net income	2,056,233,236	-	2,056,233,236
Non-controlling interest	46,498,652	-	46,498,652
Stockholder's equity	\$ 7,751,408,155	199,425,016	7,950,833,171

At December 31, 2017 and 2016, Paid-in capital includes the amount of \$11,545,094 Mexican pesos, coming from the partial capitalization of real state valuation surplus.

Variable portion of capital stock with right to reimbursement must be lower than paid in capital stock with no right to reimbursement.

According to the Law and the bylaws of the Institution: a) foreign governments or government agencies, and b) credit institutions, mutual insurance companies, brokerage firms, auxiliary credit organizations, asset management companies and broker dealers, cannot not be shareholders of the Institution, directly or through an agent.

The Ministry of Finance and Public Credit (Secretaría de Hacienda y Crédito Público or SHCP) may authorize the participation in the capital of the Institution, to insurers and reinsurers abroad as well as foreign individuals or entities other than those mentioned in the previous paragraph.

**(b) Minimum capital requirement-**

Insurance companies must maintain a minimum capital requirement for each insurance line authorized, which is also published by the Commission.

At December 31, 2017 the Institution had the minimum capital requirement amounting to \$47,402,533, equivalent to 8,521,217 investment units (UDIs, which is a unit of account whose value is updated for inflation and is determined by Central Bank) valued at 5.562883 Mexican pesos per UDI which was the value as of December 31, 2016.

**(c) Comprehensive income (CI)-**

At December 31, 2017 and 2016 the CI is analyzed on the next page.

		2017	2016
Controlling net income	\$	2,056,233,236	1,290,578,806
Surplus on property valuation		98,590,500	116,877,435
Surplus on investment valuation		(11,875,146)	-
Deferred IT and ESPS on Surplus property valuation		(19,743,951)	(46,750,974)
Employee benefits effect, net		(4,140,440)	11,753,768
Foreign currency translation adjustment on foreign operations		(33,347,834)	103,801,467
Other		(45,540)	(625,269)
Non-controlling interest		7,531,756	11,538,491
Consolidated net income	\$	2,093,202,581	1,487,173,724

**(d) Dividends-**

At the Regular General Stockholders' Meeting held on April 24, 2017, a resolution was passed to declare a dividend by the amount of \$270,000,000, \$0.6 per share, which were paid in cash through electronic transfer.

At the Regular General Stockholders' Meeting held on April 28, 2016, a resolution was passed to declare a dividend by the amount of \$225,000,000, \$0.5 per share, which were paid in cash through electronic transfer.

**(e) Restrictions on stockholders' equity-**

According to the provisions of the Law, a minimum of 10% of the income must be appropriated to the statutory reserve, up to an amount equal to the amount of paid-in capital.

According to the Commission's provisions, the unrealized gain on investment securities valuation recorded in results of operations for the year may not be distributed to stockholders until the related investments are sold, as well as deferred tax and ESPS assets recorded in income as a result of applying FRS D-4 and D-3.

Only the dividends paid to shareholders in excess of "Net Tax Income" will be subject to a tax of 30%..

**(17) Segment information--**

Information by operating segments is presented based on the management approach. In addition, condensed information by line of business and geographical area is presented.

**a) General information by line of business.**

<b>2017</b>				
	Written premium	Premium ceded	Current risk reserve	Earned retained premiums
Line of business:				
Fleets, financial institutions and other	\$ 25,381,951,785	(215,952,678)	(3,704,671,634)	21,461,327,473
Individual	6,900,702,299	-	(1,007,205,288)	5,893,497,011
Foreign	1,537,286,623	-	(224,377,629)	1,312,908,994
Total consolidated	\$ 33,819,940,707	(215,952,678)	(4,936,254,551)	28,667,733,478

<b>2016</b>				
	Written premium	Premium ceded	Current risk reserve	Earned retained premiums
Line of business:				
Fleets, financial institutions and other	\$ 24,309,873,258	(103,153,046)	(4,497,220,973)	19,709,499,239
Individual	4,426,624,511	-	(911,993,572)	3,514,630,939
Foreign	1,453,028,703	-	(852,560,627)	600,468,076
Total consolidated	\$ 30,189,526,472	(103,153,046)	(6,261,775,172)	23,824,598,254

		2017	2016
Premium receivable:			
Fleets, financial and other	\$	14,170,293,510	9,457,334,635
Individual		3,838,217,542	5,176,915,807
Foreign		336,658,820	404,443,617
Total consolidated	\$	18,345,169,872	15,038,694,059

b) General information by geographical area.

		2017	2016
Written premium:			
Mexico		32,282,654,084	28,837,166,003
United States of America		940,346,126	834,962,461
Central America		596,940,497	517,398,008
Total consolidated		33,819,940,707	30,189,526,472
Premium receivable:			
Mexico		18,008,511,053	14,634,520,442
United States of America		70,682,391	170,091,111
Central America		265,976,428	234,352,506
Total consolidated		18,345,169,872	15,038,694,059

**[18] Earnings per share-**

Earnings per share results from dividing the year's net income by outstanding shares at year end.

The Institution presents the net basic earnings per share and the diluted earnings per share. The basic earnings per share is obtained by dividing the controlling equity in the net income by the weighted average of common outstanding shares during the period, adjusted by the weighted average of shares acquired during the year. The net diluted earnings per share is determined by adjusting the weighted average of shares repurchased during the year for purposes of all the potential diluted values.



**[19] Group entities-**
**Investment in subsidiaries -**

The subsidiaries are shown on the next page.

	Ownership		Principal activity
	2017	2016	
Quálitas México	99.99%	99.99%	Practicing insurance, coinsurance and reinsurance as a property and liability insurers in the automobile line of insurance in Mexico.
Quálitas Costa Rica	99.99%	99.99%	Practicing insurance, coinsurance and reinsurance as a property and liability insurers in the automobile line of insurance in Costa Rica
Quálitas El Salvador	99.99%	99.99%	Practicing insurance, coinsurance and reinsurance as a property and liability insurers in the automobile line of insurance in El Salvador.
Quálitas Financial	100.00%	100.00%	Holding company of Quálitas Insurance, practicing insurance, coinsurance and reinsurance as a property and liability insurers in the automobile line of insurance in the United States.
Activos Jal, S. A. de C. V. (Activos Jal)	99.99%	99.99%	Property leasing and acquisition.
Cristafacil, S. A. de C. V. (Cristafacil)	56.00%	56.00%	Acquisition, sale and installation of automobile glass.
Outlet de Refacciones, S. A. de C. V. (Outlet de Refacciones)	50.86%	50.86%	Acquisition and sale of automobile spare parts.
Easy Car Glass, S. A. de C. V. (Easy Car Glass)	75.25%	75.25%	Acquisition, sale and installation of automobile glass.
Autos y salvamentos, S. A. de C. V. (Autos y salvamentos)	53.00%	51.00%	Salvage management and marketing.
Optimización de Talento, S. A. de C. V.	98.00%	-	Advisory and training services for investment planning and business management.

Significant judgments and assumptions for determining the existence of control, were as follows: Quálitas Controladora has power over its subsidiaries for directing their relevant activities by significantly influencing their decisions. In addition the executives of Quálitas Controladora are actively involved in board meetings of their subsidiaries.

Significant judgments and assumptions for identifying if the Institution is agent or principal were as follows: according to that mentioned in the preceding paragraph, Quálitas Controladora is principal being that it is the investor with power to make decisions and direct the relevant activities of its subsidiaries.

At December 31, 2017 and 2016, the investment in subsidiaries corresponding to the non-controlling interest and its equity in income for the year then ended are shown below:

December 31, 2017		<b>Non-controlling interest in stockholders' equity</b>	<b>Non-controlling interest in comprehensive income</b>
Outlet de Refacciones	\$	35,776,380	2,540,174
Easy Car Glass		3,229,475	290,738
Autos y salvamentos		5,108,589	3,522,945
Cristafácil		2,018,753	675,035
Other	\$	365,455	358,706
		46,498,652	7,387,598

December 31, 2016		<b>Non-controlling interest in stockholders' equity</b>	<b>Non-controlling interest in comprehensive income</b>
Outlet de Refacciones	\$	32,846,416	7,662,698
Easy Car Glass		2,938,737	323,258
Autos y salvamentos		1,785,357	1,626,690
Cristafácil		1,390,212	426,237
Other	\$	6,174	861
		38,966,896	10,039,744

## [20] Commitments and contingencies-

- a. The Institution is involved in a number of lawsuit and claims arising in the normal course of business. It is anticipated by the Institution's management that the final outcome of these matters will not have a significant adverse effect on the financial position and results of operations.
- b. There is a contingent liability arising from the employee benefits mentioned in note 3[0].
- c. According with Mexican tax law, the tax authorities are entitled to examine transactions carried out during the five years prior to the most recent income tax return filed.
- d. In accordance with the Income Tax Law, companies carrying out transactions with related parties are subject to certain requirements as to the determination of prices, since such prices must be similar to those that would be used in arm's-length transactions. Should the tax authorities examine the transactions and reject the related-party prices, they could assess additional taxes plus the related inflation adjustment and interest, in addition to penalties of up to 100% of the omitted taxes.

## [21] Contingent commissions-

At December 31, 2017 and 2016, the Institution executed agreements for payment of contingent commissions with intermediaries and corporations as described in this note, the total amount payments made under those agreements amounted to \$410,445,240 and \$329,752,324, accounting for 1.2% and 1.09%, respectively of the written premium by the Institution in 2017 and 2016.

Contingent commissions mean compensation or payments made to individuals or legal entities involved in intermediation or contracting of the Institution insurance products, in addition to direct compensation considered in the products design.

The Institution entered into agreements for contingent commission payments with individuals, legal entities and persons other than agents as follows:

- a. For property and casualty products, the Institution had entered into agreements related to the volume of premiums, growth and claims. The bases and criteria for participation in the agreements, and the determination of contingent commissions are directly related to the premiums paid and the claims of each year. Contingent commissions payments under these agreements are annually.
- b. For other intermediaries who are not agents, the Institution had entered compensation agreements where the bases are determined on fixed amounts that depend on the annual sales volume. Contingent commissions under such agreements are paid on a monthly basis.

The Institution or its shareholders do not hold any share in the capital of the entities with which the Institution has entered into agreements for the payment of contingent commissions.

**[22] Recently issued regulatory standards-**

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The CINIF has issued the FRS and Improvements listed below:

**FRS B-17 “Determination of fair value”-** FRS B-17 is effective for years beginning on or after January 1, 2018, allowing for early adoption, provided it takes place concurrently with the adoption of FRS C-2, C-3, C-16, C-10, C-19 and C-20. Where appropriate, changes in valuation or disclosure must be recognized prospectively. This establishes the valuation and disclosure standards in the determination of fair value, in initial and subsequent recognition, if the fair value is required or allowed by other specific FRS.

**FRS C-2 “Investment in financial instruments”-** FRS C-2 establishes specific rules for the accounting recognition of investments in financial instruments, primarily those held for trading purposes, as well as the classification of financial instruments based on the business model an entity has for all instruments as a whole. This is effective for periods beginning on or after January 1, 2018, with retrospective effects and supersedes Bulletin C-2 “Financial instruments” and the Bulletin C-2 Application guidance. Early adoption is allowed provided that it is done concurrently with the FRS related to financial instruments whose effective date and possibility for early adoption are under the same terms.

Among the principal changes presented are:

- Classification of financial instruments in which investments are made, discarding the concept of intention to acquire and use an investment in a financial instrument to determine such classification, adopting instead, the business management model of investments in financial instruments for obtaining cash flows. This change eliminates the held-to-maturity and available-for-sale categories of instruments.
- Establishing the valuation of investments in financial instruments also according to the business model, indicating that each model will have a different line item in the statement of comprehensive income.
- Not allowing the reclassification of investments in financial instruments among the categories of financial instruments

receivable, debt instruments at fair value and negotiable financial instruments, unless the entity's business model changes, which is considered highly unlikely.

- Adopting the principle that all financial instruments are valued upon initial recognition at fair value.
- Limiting certain disclosures to entities that conduct financial operations.

**FRS C-3 "Accounts receivable"**- FRS C-3 is effective for years beginning on or after January 1, 2018, with retrospective effects, except for the valuation effects that may be prospectively recognized, if it is impractical to determine the effect on each one of the prior periods presented. Early adoption is allowed provided that it takes place concurrently with the adoption of FRS related to financial instruments whose effective date and possibility for early adoption are under the same terms as those indicated in this FRS. Some of the primary changes presented are the following :

- FRS C-3 provides that accounts receivable based on a contract are deemed financial instruments, while some other accounts receivable, resulting of legal or tax provisions, may have certain characteristics of a financial instrument, such as bearing interest, but are not in themselves financial instruments.
- FRS C-3 provides that the allowance for doubtful trade receivables shall be recognized as revenue is earned, based on the expected credit losses, and the allowance shall be recorded as an expense, separately when significant, in the statement of comprehensive income.
- FRS C-3 provides that, upon initial recognition, the time value of money shall be considered. Therefore, should the effect of the present value of the account receivable be significant in light of the term, an adjustment must be made taking into consideration such present value.
- FRS C-3 requires a reconciliation between the beginning and ending balances of the allowance for doubtful accounts for each period presented.

**FRS C-9 "Provisions, Contingencies and Commitments"**- FRS C-9 is effective for years beginning on or after January 1, 2018, -allowing for early enforcement provided that it is done concurrently with the initial enforcement of FRS C-19 "Financial instruments payable". FRS C-9 supersedes Bulletin C-9 "Liabilities, Provisions, Contingent Assets and Liabilities and Commitments". The first-time adoption of this FRS does not result in accounting changes in the financial statements. Some of the primary aspects covered by this FRS include the following:

- The scope is narrowed by relocating the topic concerning accounting for financial liabilities to FRS C-19 "Financial instruments payable".
- The definition of "liability" is modified by eliminating the qualifier "virtually unavoidable" and including the term "probable".
- The terminology used throughout the standard is updated to standardize the presentation with the rest of the FRS.

**FRS C-16 "Impairment of financial instruments receivable"**- FRS C-16 is effective for years beginning on January 1, 2018 with retrospective effects and early adoption is allowed as of January 1, 2017 provided that it takes place concurrently with the adoption of FRS related to financial instruments whose effective date and early adoption are in the same terms. It establishes standards for the accounting recognition of impairment losses of all financial instruments receivable; it indicates when and how an expected impairment loss should be recognized and establishes the methodology for determination.

The primary changes arising from this FRS consist of determining when and how expected impairment losses on financial instruments receivable should be recognized, including:

- It establishes that impairment losses on financial instruments receivable should be recognized if the credit risk increases and thus it is concluded that a portion of future cash flows of the financial instruments receivable will not be recovered.
- It proposes recognizing the expected loss based on the entity's historical experience of credit losses, current conditions and reasonable and supportable forecasts of the various quantifiable future events that could affect the amount of future cash flows of the financial instruments receivable.
- With regard to interest-bearing financial instruments receivable, it establishes estimating how much of the financial instruments receivable amount is deemed recoverable and when, since the recoverable amount must be recorded at present value.

**FRS C-19 "Financial instruments payable"**- FRS C-19 is effective for years beginning on or after January 1, 2018 with retrospective effects and early adoption allowed provided that they it takes place concurrently with the adoption of FRS C-9 and the FRS related to financial instruments whose effective date and early adoption are in the same terms. Some of the main points covered by this FRS include the following:

- It provides for the possibility of measuring, subsequent to their initial recognition, certain financial liabilities at fair value when certain conditions are fulfilled.
- Long-term liabilities are initially recognized at present value.
- In restructuring a liability, without the future cash flows for its settlement being substantially modified, the costs and commissions expensed in this process shall affect the amount of the liability and be amortized on a modified effective interest rate basis instead of directly affecting net income or loss.
- It includes the provisions of IFRIC 19 "Extinguishing Financial Liabilities with Equity Instruments", which was not provided for by the existing standard.
- The effect of extinguishing a financial liability should be presented as financial income (loss) in the comprehensive statement of income.
- It introduces the concepts of amortized cost in valuing financial liabilities and of the effective interest method based on the effective interest rate.

**FRS C-20 "Financing instruments receivable"**- FRS C-20 shall be effective for years beginning January 1, 2018, and is applicable retrospectively. Early adoption is allowed provided that it takes place concurrently with the initial adoption of FRS related to financial instruments whose effective date and early adoption are in the same terms. Some of the main aspects resulting from the adoption of this FRS are as follows:

- Classification of financial instruments within assets. To determine such classification, the concept of intention to acquire and hold financial instruments has been removed. Instead, the concept of business management model is adopted, either for obtaining a contractual yield, generating a contractual yield and selling in order to achieve certain strategic objectives, or generating earnings from the purchase and sale thereof, in order to classify them in accordance with the respective model.

- The valuation effect of investments in financial instruments is also focused on the business model.
- The reclassification of financial instruments is not permitted among receivables, strategic investments, and negotiable financial instruments, unless the entity changes its business model.
- An embedded derivative that modifies the cash flows of principal and interest is not separated from its host receivable financial instrument. The entire receivable financial instrument shall be measured at fair value, as if it were a negotiable financial instrument.

**FRS D-1 “Revenue from contracts with customers”**- FRS D-1 establishes standards for the accounting recognition of revenues arising from contracts with customers and is effective for periods beginning on or after January 1, 2018 with retrospective effects, allowing for early enforcement provided that it is done concurrently with the enforcement of FRS D-2 Costs from contracts with customers”. It eliminates the supplementary application of International Accounting Standard (IAS) 18 “Revenues”, SIC 31 “Revenues – Barter transactions of advertising services”, IFRIC 13 “Customer Loyalty Programs”, and IFRIC 18 “Transfers of assets from customers”. Additionally, this FRS, along with FRS D-2, repeals Bulletin D-7 “Construction and manufacturing contracts of certain capital goods” and IFRS 14 “Construction, sales and service contracts related to real estate”. Some of the primary changes are the following:

- The transfer of control as basis for the opportunity of revenue recognition is established.
- The identification of the obligations to be fulfilled in a contract is required.
- It indicates that the transaction amount between obligations to fulfill must be assigned based on independent sales prices.
- The concept “conditional account receivable” is introduced.
- The recognition of collection rights is required.
- Requirements and guidance on how to value the variable consideration and other aspects, upon valuing the income are established.

**FRS D-2 “Costs from contracts with customers”**- FRS D-2 establishes rules for the accounting recognition of costs of sales of goods or provision of services. This is effective for periods starting on or after January 1, 2018 with retrospective effects, allowing for early enforcement provided that it is done concurrently with FRS D-1 “Revenues from contracts with customers”. Along with this FRS, it repeals Bulletin D -7 “Construction and manufacturing contracts of certain capital goods” and IFRS 14 “Construction, sales and service contracts related to real estate”, except regarding the recognition of assets and liabilities in this type of contracts within the scope of other FRS.

The primary change is the separation of the standard related to the recognition of revenues from contracts with customers, from the standard corresponding to the recognition of costs for contracts with customers. Additionally, it extends the scope of Bulletin D-7, referring exclusively to costs related to construction and manufacturing contracts for certain capital goods, to include costs related to all types of contracts with customers.

## 2018 FRS Revisions

In December 2017, CINIF issued a document called “2018 FRS Revisions” containing precise modifications to some of the existing FRS. The main revisions that bring about accounting changes are the following:

**FRS B-2 “Statement of cash flows”**- Requires new disclosures about liabilities associated with financing activities, whether or not, they have required the use of cash or cash equivalents, preferably through a reconciliation of the initial and final balances thereof. This revision will be effective for periods starting on or after January 1, 2018, allowing early adoption. The resulting accounting changes should be recognized retrospectively.

**FRS C-6 “Property, plant and equipment” and FRS C-8 “Intangible assets”**- Establishes that a method of depreciation and amortization of an asset based on the generation of economic benefits associated with its use is not appropriate, given that said amount may be affected by factors other than the pattern of consumption of economic benefits of the asset. Clarifies the meaning of the concept of consumption of future economic benefits of an asset. This revision will be effective for periods starting on or after January 1, 2018, allowing early adoption. The resulting accounting changes should be recognized prospectively.

**FRS C-14 “Transfer and derecognition of financial assets”**- Eliminates the requirement to recognize in earnings the effects of the subsequent recognition at fair value of a transferred asset and of the associated liability since it represented a contradiction with the requirement in the same standard that said recognition be made based on the relative rules, depending on the type of asset in question. This revision will be effective for periods starting on or after January 1, 2018, allowing early adoption. The resulting accounting changes should be recognized retrospectively.

Management estimates that the new FRS and revisions to FRS not generate significant effects on the financial information of the Institution. The effects of the new FRS and the revisions to FRS 2017 will depend on its adoption by the Commission.

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