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

# FORM 10-Q

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

**For the quarterly period ended September 30, 2019**

**OR**

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

**For the transition period from __________ to __________**

**Commission file number 1-5975**

# HUMANA INC.

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Delaware** | **61-0647538** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |

**500 West Main Street**
**Louisville, Kentucky 40202**
**(Address of principal executive offices, including zip code)**

**(502) 580-1000**
**(Registrant's telephone number, including area code)**

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

| Title of each class | Trading Symbol | Name of each exchange on which registered |
|---|---|---|
| Common stock, $0.16 2/3 par value | HUM | New York Stock Exchange |

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes ☒  No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).  Yes ☒  No ☐

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

| | | | |
|---|---|---|---|
| Large accelerated filer | ☒ | Accelerated filer | ☐ |
| Non-accelerated filer | ☐ | Smaller reporting company | ☐ |
| Emerging growth company | ☐ | | |

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).  Yes ☐  No ☒

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

| Class of Common Stock | Outstanding at September 30, 2019 |
|---|---|
| $0.16 2/3 par value | 132,426,045 shares |

**Humana Inc.**
FORM 10-Q
SEPTEMBER 30, 2019

## INDEX

**Humana Inc.**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**(Unaudited)**

| | September 30, 2019 | December 31, 2018 |
|---|---|---|
| | (in millions, except share amounts) | |
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 5,527 | $ 2,343 |
| Investment securities | 10,430 | 10,026 |
| Receivables, less allowance for doubtful accounts of $73 in 2019 and $79 in 2018 | 848 | 1,015 |
| Other current assets | 3,519 | 3,564 |
| Total current assets | 20,324 | 16,948 |
| Property and equipment, net | 1,864 | 1,735 |
| Long-term investment securities | 404 | 411 |
| Equity method investment in Kindred at Home | 1,061 | 1,047 |
| Goodwill | 3,922 | 3,897 |
| Other long-term assets | 1,605 | 1,375 |
| Total assets | $ 29,180 | $ 25,413 |
| **LIABILITIES AND STOCKHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Benefits payable | $ 6,220 | $ 4,862 |
| Trade accounts payable and accrued expenses | 3,640 | 3,067 |
| Book overdraft | 273 | 171 |
| Unearned revenues | 274 | 283 |
| Short-term debt | 699 | 1,694 |
| Total current liabilities | 11,106 | 10,077 |
| Long-term debt | 5,365 | 4,375 |
| Future policy benefits payable | 211 | 219 |
| Other long-term liabilities | 897 | 581 |
| Total liabilities | 17,579 | 15,252 |
| Commitments and contingencies (Note 14) | | |
| Stockholders' equity: | | |
| Preferred stock, $1 par; 10,000,000 shares authorized; none issued | — | — |
| Common stock, $0.16 2/3 par; 300,000,000 shares authorized; 198,628,992 shares issued at September 30, 2019 and 198,594,841 shares issued at December 31, 2018 | 33 | 33 |
| Capital in excess of par value | 2,608 | 2,535 |
| Retained earnings | 17,045 | 15,072 |
| Accumulated other comprehensive income (loss) | 177 | (159) |
| Treasury stock, at cost, 66,202,947 shares at September 30, 2019 and 63,028,169 shares at December 31, 2018 | (8,262) | (7,320) |
| Total stockholders' equity | 11,601 | 10,161 |
| Total liabilities and stockholders' equity | $ 29,180 | $ 25,413 |

See accompanying notes to condensed consolidated financial statements.

**Humana Inc.**
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**
**(Unaudited)**

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| | (in millions, except per share results) | | | |
| Revenues: | | | | |
| Premiums | $ 15,712 | $ 13,712 | $ 47,139 | $ 41,236 |
| Services | 393 | 381 | 1,103 | 1,090 |
| Investment income | 136 | 113 | 351 | 418 |
| Total revenues | 16,241 | 14,206 | 48,593 | 42,744 |
| Operating expenses: | | | | |
| Benefits | 13,357 | 11,243 | 40,168 | 34,449 |
| Operating costs | 1,889 | 1,900 | 5,252 | 5,410 |
| Depreciation and amortization | 127 | 102 | 343 | 302 |
| Total operating expenses | 15,373 | 13,245 | 45,763 | 40,161 |
| Income from operations | 868 | 961 | 2,830 | 2,583 |
| (Gain) loss on sale of business | — | (4) | — | 786 |
| Interest expense | 62 | 53 | 184 | 159 |
| Other (income) expense, net | (82) | 11 | (217) | 11 |
| Income before income taxes and equity in net earnings | 888 | 901 | 2,863 | 1,627 |
| Provision for income taxes | 200 | 266 | 684 | 308 |
| Equity in net earnings of Kindred at Home | 1 | 9 | 16 | 9 |
| Net income | $ 689 | $ 644 | $ 2,195 | $ 1,328 |
| Basic earnings per common share | $ 5.16 | $ 4.68 | $ 16.31 | $ 9.64 |
| Diluted earnings per common share | $ 5.14 | $ 4.65 | $ 16.24 | $ 9.58 |

See accompanying notes to condensed consolidated financial statements.

**Humana Inc.**
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**(Unaudited)**

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| | (in millions) | | | |
| Net income | $ 689 | $ 644 | $ 2,195 | $ 1,328 |
| Other comprehensive income: | | | | |
| Change in gross unrealized investment gains/losses | 87 | (42) | 452 | (254) |
| Effect of income taxes | (20) | 10 | (105) | 64 |
| Total change in unrealized investment gains/losses, net of tax | 67 | (32) | 347 | (190) |
| Reclassification adjustment for net realized gains | (1) | 3 | (7) | (49) |
| Effect of income taxes | — | (1) | 2 | 14 |
| Total reclassification adjustment, net of tax | (1) | 2 | (5) | (35) |
| Other comprehensive income (loss), net of tax | 66 | (30) | 342 | (225) |
| Comprehensive loss attributable to equity method investment in Kindred at Home | (1) | — | (6) | — |
| Comprehensive income | $ 754 | $ 614 | $ 2,531 | $ 1,103 |

See accompanying notes to condensed consolidated financial statements.

**Humana Inc.**
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**
**(Unaudited)**

| | Common Stock | | Capital In Excess of Par Value | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Treasury Stock | Total Stockholders' Equity |
|---|---|---|---|---|---|---|---|
| | Issued Shares | Amount | | | | | |
| | | | (dollars in millions, share amounts in thousands) | | | | |
| **Three months ended September 30, 2019** | | | | | | | |
| Balances, June 30, 2019 | 198,628 | $ 33 | $ 2,763 | $ 16,429 | $ 112 | $ (7,465) | $ 11,872 |
| Net income | | | | 689 | | | 689 |
| Other comprehensive income | | | | | 65 | | 65 |
| Common stock repurchases | | | (200) | | | (800) | (1,000) |
| Dividends and dividend equivalents | | | — | (73) | | | (73) |
| Stock-based compensation | | | 43 | | | | 43 |
| Restricted stock unit vesting | — | — | | | | — | — |
| Stock option exercises | 1 | — | 2 | | | 3 | 5 |
| Balances, September 30, 2019 | 198,629 | $ 33 | $ 2,608 | $ 17,045 | $ 177 | $ (8,262) | $ 11,601 |
| | | | | | | | |
| **Three months ended September 30, 2018** | | | | | | | |
| Balances, June 30, 2018 | 198,591 | $ 33 | $ 2,672 | $ 14,211 | $ (176) | $ (6,529) | $ 10,211 |
| Net income | | | | 644 | | | 644 |
| Other comprehensive loss | | | | | (30) | | (30) |
| Common stock repurchases | | | — | | | (201) | (201) |
| Dividends and dividend equivalents | | | — | (69) | | | (69) |
| Stock-based compensation | | | 35 | | | | 35 |
| Restricted stock unit vesting | — | — | (3) | | | 3 | — |
| Stock option exercises | 2 | — | 3 | | | — | 3 |
| Balances, September 30, 2018 | 198,593 | $ 33 | $ 2,707 | $ 14,786 | $ (206) | $ (6,727) | $ 10,593 |

See accompanying notes to condensed consolidated financial statements.

**Humana Inc.**
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS’ EQUITY**
**(Unaudited)**

| | Common Stock | | | | | | |
|---|---|---|---|---|---|---|---|
| | Issued Shares | Amount | Capital In Excess of Par Value | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Treasury Stock | Total Stockholders’ Equity |
| | (dollars in millions, share amounts in thousands) | | | | | | |
| **Nine months ended September 30, 2019** | | | | | | | |
| Balances, December 31, 2018 | 198,595 | $ 33 | $ 2,535 | $ 15,072 | $ (159) | $ (7,320) | $ 10,161 |
| Net income | | | | 2,195 | | | 2,195 |
| Other comprehensive income | | | | — | 336 | | 336 |
| Common stock repurchases | | | (50) | | | (960) | (1,010) |
| Dividends and dividend equivalents | | | — | (222) | | . | (222) |
| Stock-based compensation | | | 119 | | | | 119 |
| Restricted stock unit vesting | 32 | — | (3) | | | 3 | — |
| Stock option exercises | 2 | — | 7 | | | 15 | 22 |
| Balances, September 30, 2019 | 198,629 | $ 33 | $ 2,608 | $ 17,045 | $ 177 | $ (8,262) | $ 11,601 |
| **Nine months ended September 30, 2018** | | | | | | | |
| Balances, December 31, 2017 | 198,572 | $ 33 | $ 2,445 | $ 13,670 | $ 19 | $ (6,325) | $ 9,842 |
| Net income | | | | 1,328 | | | 1,328 |
| Other comprehensive loss | | | | (4) | (225) | | (229) |
| Common stock repurchases | | | 200 | | | (494) | (294) |
| Dividends and dividend equivalents | | | — | (208) | | | (208) |
| Stock-based compensation | | | 105 | | | | 105 |
| Restricted stock unit vesting | — | — | (92) | | | 92 | — |
| Stock option exercises | 21 | — | 49 | | | — | 49 |
| Balances, September 30, 2018 | 198,593 | $ 33 | $ 2,707 | $ 14,786 | $ (206) | $ (6,727) | $ 10,593 |

See accompanying notes to condensed consolidated financial statements.

**Humana Inc.**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(Unaudited)**

| | For the nine months ended September 30, | |
|---|---|---|
| | 2019 | 2018 |
| | (in millions) | |
| **Cash flows from operating activities** | | |
| Net income | $ 2,195 | $ 1,328 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Loss on sale of business | — | 786 |
| Net realized capital gains | (23) | (90) |
| Equity in net earnings of Kindred at Home | (16) | (9) |
| Stock-based compensation | 119 | 105 |
| Depreciation | 382 | 330 |
| Amortization | 53 | 70 |
| (Benefit) provision for deferred income taxes | (21) | 165 |
| Changes in operating assets and liabilities, net of effect of businesses acquired and dispositions: | | |
| Receivables | 179 | (211) |
| Other assets | 334 | (939) |
| Benefits payable | 1,358 | 410 |
| Other liabilities | 168 | 548 |
| Unearned revenues | (9) | (84) |
| Other | 53 | 97 |
| Net cash provided by operating activities | 4,772 | 2,506 |
| **Cash flows from investing activities** | | |
| Cash transferred in sale of business | — | (805) |
| Acquisitions, net of cash acquired | — | (354) |
| Acquisition, equity method investment in Kindred at Home | — | (1,095) |
| Purchases of property and equipment | (506) | (436) |
| Purchases of investment securities | (4,130) | (3,379) |
| Maturities of investment securities | 1,281 | 815 |
| Proceeds from sales of investment securities | 2,878 | 2,614 |
| Net cash used in investing activities | (477) | (2,640) |
| **Cash flows from financing activities** | | |
| Receipts from contract deposits, net | 11 | 378 |
| Proceeds from issuance of senior notes, net | 987 | — |
| (Repayments) proceeds from issuance of commercial paper, net | (358) | 240 |
| Repayment of term loan | (650) | — |
| Change in book overdraft | 102 | 58 |
| Common stock repurchases | (1,010) | (294) |
| Dividends paid | (216) | (195) |
| Proceeds from stock option exercises and other, net | 23 | 47 |
| Net cash (used in) provided by financing activities | (1,111) | 234 |
| Increase in cash and cash equivalents | 3,184 | 100 |
| Cash and cash equivalents at beginning of period | 2,343 | 4,042 |
| Cash and cash equivalents at end of period | $ 5,527 | $ 4,142 |
| **Supplemental cash flow disclosures:** | | |
| Interest payments | $ 136 | $ 120 |
| Income tax payments, net | $ 578 | $ 511 |

See accompanying notes to condensed consolidated financial statements.

**Humana Inc.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(Unaudited)**

## 1. BASIS OF PRESENTATION AND SIGNIFICANT EVENTS

The accompanying condensed consolidated financial statements are presented in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America, or GAAP, or those normally made in an Annual Report on Form 10-K. The year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. For further information, the reader of this Form 10-Q should refer to our Form 10-K for the year ended December 31, 2018, that was filed with the Securities and Exchange Commission, or the SEC, on February 21, 2019. We refer to the Form 10-K as the “2018 Form 10-K” in this document. References throughout this document to “we,” “us,” “our,” “Company,” and “Humana” mean Humana Inc. and its subsidiaries.

The preparation of our condensed consolidated financial statements in accordance with GAAP requires us to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. The areas involving the most significant use of estimates are the estimation of benefits payable, the impact of risk adjustment provisions related to our Medicare contracts, the valuation and related impairment recognition of investment securities, and the valuation and related impairment recognition of long-lived assets, including goodwill. These estimates are based on knowledge of current events and anticipated future events, and accordingly, actual results may ultimately differ materially from those estimates. Refer to Note 2 to the consolidated financial statements included in our 2018 Form 10-K for information on accounting policies that we consider in preparing our consolidated financial statements.

The financial information has been prepared in accordance with our customary accounting practices and has not been audited. In our opinion, the information presented reflects all adjustments necessary for a fair statement of interim results. All such adjustments are of a normal and recurring nature.

***Revenue Recognition***

Our revenues include premium and service revenues. Service revenues include administrative service fees that are recorded based upon established per member per month rates and the number of members for the month and are recognized as services are provided for the month. Additionally, service revenues include net patient service revenues that are recorded based upon established billing rates, less allowances for contractual adjustments, and are recognized as services are provided. For more information about our revenues, refer to Note 2 to the consolidated financial statements included in our 2018 Form 10-K for information on accounting policies that we consider in preparing our consolidated financial statements. See Note 15 for disaggregation of revenue by segment and type.

At September 30, 2019, accounts receivable related to services were $141 million. For the three and nine months ended September 30, 2019, we had no material bad-debt expense and there were no material contract assets, contract liabilities or deferred contract costs recorded on the condensed consolidated balance sheet at September 30, 2019.

For the three and nine months ended September 30, 2019, services revenue recognized from performance obligations related to prior periods (for example, due to changes in transaction price), was not material. Further, services revenue expected to be recognized in any future year related to remaining performance obligations was not material.

***Equity Method Investment in Kindred at Home***

In the third quarter of 2018, we, along with TPG Capital, or TPG, and Welsh, Carson, Anderson & Stowe, or WCAS, completed the acquisitions of Kindred Healthcare, Inc., or Kindred, and privately-held Curo Health Services, or Curo, respectively, merging Curo with the hospice business of the Kindred at Home Division, or Kindred at Home. As part of these transactions, we acquired a 40% minority interest in Kindred at Home, a leading home health and hospice company, for total cash consideration of approximately $1.1 billion.

We account for our 40% investment in Kindred at Home using the equity method of accounting. This investment is reflected as "Equity method investment in Kindred at Home" in our condensed consolidated balance sheets, with our share of income or loss reported as "Equity in net earnings of Kindred at Home" in our condensed consolidated statements of income.

We entered into a shareholders agreement with TPG and WCAS, the Sponsors, that provides for certain rights and obligations of each party. The shareholders agreement with the Sponsors includes a put option under which they have the right to require us to purchase their interest in the joint venture beginning on July 2, 2021 and ending on July 1, 2022. Likewise, we have a call option under which we have the right to require the Sponsors to sell their interest in the joint venture to Humana beginning on July 2, 2022 and ending on July 1, 2023. The put and call options, which are exercisable at a fixed EBITDA multiple and provide a minimum return on the Sponsor's investment if exercised, are measured at fair value each period using a Monte Carlo simulation. The simulation relies on assumptions around Kindred at Home's equity value, risk free interest rates, volatility, and the details specific to the put and call options. The final purchase price allocation resulted in approximately $1 billion being allocated to the investment and $236 million and $291 million allocated to the put and call options, respectively. The fair values of the put option and call option were $90 million and $327 million, respectively, at September 30, 2019. The put option is included within other long-term liabilities and the call option is included within other long-term assets. The change in fair value of the put and call options is reflected as "Other (income) expense, net" in our condensed consolidated statements of income.

***Health Care Reform***

The Patient Protection and Affordable Care Act and The Health Care and Education Reconciliation Act of 2010 (which we collectively refer to as the Health Care Reform Law) enacted significant reforms to various aspects of the U.S. health insurance industry. Certain of these reforms became effective January 1, 2014, including an annual insurance industry premium-based fee. The Continuing Resolution bill, H.R. 195, enacted on January 22, 2018, included a one year suspension in 2019 of the health insurance industry fee, but under current law, the fee is scheduled to resume in calendar year 2020. In October 2018, we paid the federal government $1.04 billion for the annual health insurance industry fee attributed to calendar year 2018. This fee, fixed in amount by law and apportioned to insurance carriers based on market share, was not deductible for tax purposes. Each year on January 1, except when suspended, we record a liability for this fee in trade accounts payable and accrued expenses which we carry until the fee is paid. We record a corresponding deferred cost in other current assets in our condensed consolidated financial statements which is amortized ratably to expense over the calendar year. Amortization of the deferred cost was recorded in operating cost expense of approximately $258 million and $778 million for the three and nine months ended September 30, 2018, respectively, resulting from the amortization of the 2018 annual health insurance industry fee.

## 2. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In February 2016, the FASB issued new guidance related to accounting for leases which requires lessees to record assets and liabilities reflecting the leased assets and lease obligations, respectively, while following the dual model for recognition in statements of income requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). We adopted the new standard effective January 1, 2019, as allowed, using the modified retrospective approach. We elected the practical expedients of not reassessing whether any expired or existing contracts are or contain leases, not reassessing the lease classification for any expired or existing leases and not reassessing any initial direct costs for existing leases. In addition, we elected the practical expedient to not separate lease and nonlease components for all of our asset classes. We made a permitted accounting policy election to not apply the new guidance to leases with an initial term of 12 months or less. We recognize those lease payments in the condensed consolidated statement of income on a straight-line basis over the lease term. As of January 1, 2019, the adoption of the standard resulted in recognition of right-of-use, or ROU, liabilities of approximately $470 million and ROU assets of $436 million, which equals the ROU liabilities net of accrued rent and lease incentives. The standard does not materially affect our results of operations, cash flows and liquidity. See Note 8 for further information.

In June 2016, the FASB issued guidance introducing a new model for recognizing credit losses on financial instruments based on an estimate of current expected credit losses. The guidance is effective for us beginning January

1, 2020. The new current expected credit losses (CECL) model generally calls for the immediate recognition of all expected credit losses and applies to loans, accounts and trade receivables as well as other financial assets measured at amortized cost, loan commitments and off-balance sheet credit exposures, debt securities and other financial assets measured at fair value through other comprehensive income, and beneficial interests in securitized financial assets. The new guidance replaces the current incurred loss model for measuring expected credit losses, requires expected losses on available for sale debt securities to be recognized through an allowance for credit losses rather than as reductions in the amortized cost of the securities, and provides for additional disclosure requirements. Our investment portfolio consists of available for sale debt securities. We have identified and are analyzing our financial assets measured at amortized cost that are in scope of the new CECL model. We continue to consider the impact of the modified impairment model as it relates to our available for sale debt securities. We continue to analyze and evaluate these impacts on our results of operations, financial condition, and cash flows.

In March 2017, the FASB issued new guidance that amends the accounting for premium amortization on purchased callable debt securities by shortening the amortization period. This amended guidance requires the premium to be amortized to the earliest call date instead of maturity date. The new guidance is effective for us beginning with annual and interim periods in 2019. This guidance did not have a material impact on our results of operations, financial condition or cash flows.

In September 2018, the FASB issued new guidance related to accounting for long-duration contracts of insurers which revises key elements of the measurement models and disclosure requirements for long-duration contracts issued by insurers and reinsurers. The new guidance is effective for us beginning with annual and interim periods in 2021, with earlier adoption permitted, and requires retrospective application to previously issued annual and interim financial statements. The FASB has recently proposed delaying the effective date beginning with annual and interim periods in 2022. We are currently evaluating the impact on our results of operations, financial position and cash flows.

There are no other recently issued accounting standards that apply to us or that are expected to have a material impact on our results of operations, financial condition, or cash flows.

## 3. ACQUISITIONS AND DIVESTITURES

***Sale of Closed Block of Commercial Long-Term Care Insurance Business***

In the third quarter of 2018, we completed the sale of our wholly-owned subsidiary, KMG America Corporation, or KMG, to Continental General Insurance Company, or CGIC, a Texas-based insurance company wholly owned by HC2 Holdings, Inc., a diversified holding company. KMG's subsidiary, Kanawha Insurance Company, or KIC, included our closed block of non-strategic commercial long-term care policies. Upon closing, we funded the transaction with approximately $190 million of parent company cash contributed into KMG, subject to customary adjustments, in addition to the transfer of approximately $160 million of statutory capital with the sale.

In connection with the sale of KMG, we recognized a pretax loss, including transaction costs, of $786 million and a corresponding $452 million income tax benefit.

Also, in the third quarter of 2018, we entered into reinsurance contracts to transfer the risk associated with certain voluntary benefit and financial protection products previously issued primarily by KIC to a third party. We transferred approximately $245 million of cash to the third party and recorded a commensurate reinsurance recoverable as a result of these transactions. The reinsurance recoverable was included as part of the net assets disposed. There was no material impact to operating results from these reinsurance transactions.

KMG revenues and pretax income for the nine months ended September 30, 2018 were $182 million and $47 million, respectively. KMG revenues and pretax loss for the three months ended September 30, 2018 were not material.

***Other Acquisitions and Divestitures***

In the first quarter of 2018, we acquired the remaining equity interest in MCCI Holdings, LLC, or MCCI, a privately held management service organization headquartered in Miami, Florida, that primarily coordinates medical care for Medicare Advantage beneficiaries in Florida and Texas. The purchase price consisted primarily of $169 million cash, as well as our existing investment in MCCI and a note receivable and a revolving note with an aggregate balance of $383 million. This resulted in a purchase price allocation to goodwill of $483 million, other intangible assets of $80 million, and net tangible assets of $24 million. The goodwill was assigned to the Retail and Healthcare Services segments. The other intangible assets, which primarily consist of customer contracts, have an estimated weighted average useful life of 8 years. Goodwill and other intangible assets are amortizable as deductible expenses for tax purposes.

In the second quarter of 2018, we acquired Family Physicians Group, or FPG, for cash consideration of approximately $185 million, net of cash received. FPG serves Medicare Advantage and Managed Medicaid HMO patients in Greater Orlando, Florida with a footprint that includes clinics located in Lake, Orange, Osceola and Seminole counties. This resulted in a purchase price allocation to goodwill of $133 million, other intangible assets of $38 million and net tangible assets of $14 million. The goodwill was assigned to the Retail and Healthcare Services segments. The other intangible assets, which primarily consist of customer contracts, have an estimated weighted average useful life of 4.9 years. The purchase price allocations for MCCI and FPG are final.

During 2019 and 2018, we acquired other health and wellness related businesses which, individually or in the aggregate, have not had a material impact on our results of operations, financial condition, or cash flows. The results of operations and financial condition of these businesses have been included in our condensed consolidated statements of income and condensed consolidated balance sheets from the respective acquisition dates. Acquisition-related costs recognized in 2019 and 2018 were not material to our results of operations. The pro forma financial information assuming the acquisitions had occurred as of the beginning of the calendar year prior to the year of acquisition, as well as the revenues and earnings generated during the year of acquisition, were not material for disclosure purposes.

**Humana Inc.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**
**(Unaudited)**

## 4. INVESTMENT SECURITIES

Investment securities classified as current and long-term were as follows at September 30, 2019 and December 31, 2018, respectively:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| | | (in millions) | | |
| **September 30, 2019** | | | | |
| U.S. Treasury and other U.S. government corporations and agencies: | | | | |
| U.S. Treasury and agency obligations | $ 373 | $ 2 | $ (1) | $ 374 |
| Mortgage-backed securities | 3,543 | 101 | (3) | 3,641 |
| Tax-exempt municipal securities | 1,465 | 36 | — | 1,501 |
| Mortgage-backed securities: | | | | |
| Residential | — | — | — | — |
| Commercial | 641 | 27 | — | 668 |
| Asset-backed securities | 1,030 | 3 | (3) | 1,030 |
| Corporate debt securities | 3,509 | 84 | (3) | 3,590 |
| Total debt securities | $ 10,561 | $ 253 | $ (10) | $ 10,804 |

We held $30 million of equity securities as of September 30, 2019 consisting of common stock.

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| **December 31, 2018** | | | | |
| U.S. Treasury and other U.S. government corporations and agencies: | | | | |
| U.S. Treasury and agency obligations | $ 419 | $ 1 | $ (3) | $ 417 |
| Mortgage-backed securities | 2,595 | 3 | (54) | 2,544 |
| Tax-exempt municipal securities | 2,805 | 3 | (37) | 2,771 |
| Mortgage-backed securities: | | | | |
| Residential | 55 | — | — | 55 |
| Commercial | 537 | — | (14) | 523 |
| Asset-backed securities | 991 | 1 | (7) | 985 |
| Corporate debt securities | 3,239 | 1 | (98) | 3,142 |
| Total debt securities | $ 10,641 | $ 9 | $ (213) | $ 10,437 |

**Humana Inc.**
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Gross unrealized losses and fair values aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position were as follows at September 30, 2019 and December 31, 2018, respectively:

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| | (in millions) | | | | | |
| **September 30, 2019** | | | | | | |
| U.S. Treasury and other U.S. government corporations and agencies: | | | | | | |
| U.S. Treasury and agency obligations | $ 31 | $ — | $ 21 | $ (1) | $ 52 | $ (1) |
| Mortgage-backed securities | 122 | (1) | 269 | (2) | 391 | (3) |
| Tax-exempt municipal securities | — | — | 207 | — | 207 | — |
| Mortgage-backed securities: | | | | | | |
| Residential | — | — | — | — | — | — |
| Commercial | 24 | — | 55 | — | 79 | — |
| Asset-backed securities | 196 | (1) | 420 | (2) | 616 | (3) |
| Corporate debt securities | 261 | (1) | 191 | (2) | 452 | (3) |
| Total debt securities | $ 634 | $ (3) | $ 1,163 | $ (7) | $ 1,797 | $ (10) |
| **December 31, 2018** | | | | | | |
| U.S. Treasury and other U.S. government corporations and agencies: | | | | | | |
| U.S. Treasury and agency obligations | $ 179 | $ (1) | $ 153 | $ (2) | $ 332 | $ (3) |
| Mortgage-backed securities | 956 | (16) | 1,019 | (38) | 1,975 | (54) |
| Tax-exempt municipal securities | 809 | (9) | 1,648 | (28) | 2,457 | (37) |
| Mortgage-backed securities: | | | | | | |
| Residential | — | — | 15 | — | 15 | — |
| Commercial | 372 | (8) | 133 | (6) | 505 | (14) |
| Asset-backed securities | 824 | (7) | 40 | — | 864 | (7) |
| Corporate debt securities | 1,434 | (35) | 1,439 | (63) | 2,873 | (98) |
| Total debt securities | $ 4,574 | $ (76) | $ 4,447 | $ (137) | $ 9,021 | $ (213) |

Approximately 96% of our debt securities were investment-grade quality, with a weighted average credit rating of AA by Standard & Poor's Rating Service, or S&P, at September 30, 2019. Most of the debt securities that were below investment-grade were rated BB, the higher end of the below investment-grade rating scale. Tax-exempt municipal securities were diversified among general obligation bonds of states and local municipalities in the United States as well as special revenue bonds issued by municipalities to finance specific public works projects such as utilities, water and sewer, transportation, or education. Our general obligation bonds are diversified across the United States with no individual state exceeding 1% of our total debt securities. Our investment policy limits investments in a single issuer and requires diversification among various asset types.

Our unrealized losses from all securities were generated from approximately 250 positions out of a total of approximately 1,530 positions at September 30, 2019. All issuers of securities we own that were trading at an unrealized loss at September 30, 2019 remain current on all contractual payments. After taking into account these and other factors previously described, we believe these unrealized losses primarily were caused by an increase in market interest rates in the current markets since the time the securities were purchased. At September 30, 2019, we did not intend to sell the securities with an unrealized loss position in accumulated other comprehensive income, and it is not likely that we will be required to sell these securities before recovery of their amortized cost basis. As a result, we believe that the securities with an unrealized loss were not other-than-temporarily impaired at September 30, 2019.

The detail of realized gains (losses) related to investment securities and included within investment income was as follows for the three and nine months ended September 30, 2019 and 2018:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| | (in millions) | | | |
| Gross realized gains | $ 41 | $ 10 | $ 59 | $ 105 |
| Gross realized losses | (23) | (2) | (36) | (15) |
| Net realized capital (losses) gains | $ 18 | $ 8 | $ 23 | $ 90 |

There were no material other-than-temporary impairments for the three and nine months ended September 30, 2019 or 2018.

The contractual maturities of debt securities available for sale at September 30, 2019, regardless of their balance sheet classification, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Amortized Cost | Fair Value |
|---|---|---|
| | (in millions) | |
| Due within one year | $ 839 | $ 840 |
| Due after one year through five years | 2,277 | 2,312 |
| Due after five years through ten years | 1,730 | 1,789 |
| Due after ten years | 501 | 524 |
| Mortgage and asset-backed securities | 5,214 | 5,339 |
| Total debt securities | $ 10,561 | $ 10,804 |

**Humana Inc.**
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## 5. FAIR VALUE

***Financial Assets***

The following table summarizes our fair value measurements at September 30, 2019 and December 31, 2018, respectively, for financial assets measured at fair value on a recurring basis:

| | Fair Value | Fair Value Measurements Using: Quoted Prices in Active Markets (Level 1) | Other Observable Inputs (Level 2) | Unobservable Inputs (Level 3) |
|---|---|---|---|---|
| | (in millions) | | | |
| **September 30, 2019** | | | | |
| Cash equivalents | $ 5,015 | $ 5,015 | $ — | $ — |
| Debt securities: | | | | |
| U.S. Treasury and other U.S. government corporations and agencies: | | | | |
| U.S. Treasury and agency obligations | 374 | — | 374 | — |
| Mortgage-backed securities | 3,641 | — | 3,641 | — |
| Tax-exempt municipal securities | 1,501 | — | 1,501 | — |
| Mortgage-backed securities: | | | | |
| Residential | — | — | — | — |
| Commercial | 668 | — | 668 | — |
| Asset-backed securities | 1,030 | — | 1,030 | — |
| Corporate debt securities | 3,590 | — | 3,590 | — |
| Total debt securities | 10,804 | — | 10,804 | — |
| Common stock | 30 | 30 | — | — |
| Total invested assets | $ 15,849 | $ 5,045 | $ 10,804 | $ — |
| **December 31, 2018** | | | | |
| Cash equivalents | $ 2,024 | $ 2,024 | $ — | $ — |
| Debt securities: | | | | |
| U.S. Treasury and other U.S. government corporations and agencies: | | | | |
| U.S. Treasury and agency obligations | 417 | — | 417 | — |
| Mortgage-backed securities | 2,544 | — | 2,544 | — |
| Tax-exempt municipal securities | 2,771 | — | 2,771 | — |
| Mortgage-backed securities: | | | | |
| Residential | 55 | — | 55 | — |
| Commercial | 523 | — | 523 | — |
| Asset-backed securities | 985 | — | 985 | — |
| Corporate debt securities | 3,142 | — | 3,142 | — |
| Total debt securities | 10,437 | — | 10,437 | — |
| Total invested assets | $ 12,461 | $ 2,024 | $ 10,437 | $ — |

***Financial Liabilities***

Our debt is recorded at carrying value in our consolidated balance sheets. The carrying value of our senior notes debt outstanding, net of unamortized debt issuance costs, was $5,765 million at September 30, 2019 and $4,774 million at December 31, 2018. The fair value of our senior notes debt was $6,246 million at September 30, 2019 and $5,191 million at December 31, 2018. The fair value of our long-term debt is determined based on Level 2 inputs, including quoted market prices for the same or similar debt, or if no quoted market prices are available, on the current prices estimated to be available to us for debt with similar terms and remaining maturities. Due to the short-term nature, carrying value approximates fair value for our commercial paper borrowings and term note. The outstanding commercial paper borrowings were $299 million as of September 30, 2019 and we repaid the term note balance in August 2019. The term loan outstanding and commercial paper borrowings were $1,295 million as of December 31, 2018.

***Other Assets and Liabilities Measured at Fair Value***

As disclosed in Note 3, we acquired MCCI and FPG during 2018. The values of net tangible assets acquired and the resulting goodwill and other intangible assets were recorded at fair value using Level 3 inputs. The majority of the tangible assets acquired and liabilities assumed were recorded at their carrying values as of the respective dates of acquisition, as their carrying values approximated their fair values due to their short-term nature. The fair values of goodwill and other intangible assets acquired in these acquisitions were internally estimated primarily based on the income approach. The income approach estimates fair value based on the present value of the cash flows that the assets are expected to generate in the future. We developed internal estimates for the expected future cash flows and discount rates used in the present value calculations. Other than assets acquired and liabilities assumed in these acquisitions, and the put option liability and call option asset associated with our investment in Kindred at Home as detailed in Note 1, there were no other material assets or liabilities measured at fair value on a recurring or nonrecurring basis during 2019 or 2018.

## 6. MEDICARE PART D

We cover prescription drug benefits in accordance with Medicare Part D under multiple contracts with the Centers for Medicare and Medicaid Services, or CMS, as described further in Note 2 to the consolidated financial statements included in our 2018 Form 10-K. The accompanying condensed consolidated balance sheets include the following amounts associated with Medicare Part D at September 30, 2019 and December 31, 2018. CMS subsidies/discounts in the table below include the reinsurance and low-income cost subsidies funded by CMS for which we assume no risk as well as brand name prescription drug discounts for Part D plan participants in the coverage gap funded by CMS and pharmaceutical manufacturers.

| | September 30, 2019 | | December 31, 2018 | |
|---|---|---|---|---|
| | Risk Corridor Settlement | CMS Subsidies/ Discounts | Risk Corridor Settlement | CMS Subsidies/ Discounts |
| | (in millions) | | | |
| Other current assets | $ 11 | $ 337 | $ 15 | $ 172 |
| Trade accounts payable and accrued expenses | (49) | (781) | (103) | (503) |
| Net current liability | (38) | (444) | (88) | (331) |
| Other long-term assets | 25 | — | 7 | — |
| Other long-term liabilities | (142) | — | (89) | — |
| Net long-term liability | (117) | — | (82) | — |
| Total net liability | $ (155) | $ (444) | $ (170) | $ (331) |

## 7. GOODWILL AND OTHER INTANGIBLE ASSETS

Changes in the carrying amount of goodwill for our reportable segments for the nine months ended September 30, 2019 were as follows:

| | Retail | Group and Specialty | Healthcare Services | Total |
|---|---|---|---|---|
| | (in millions) | | | |
| Balance at January 1, 2019 | $ 1,535 | $ 261 | $ 2,101 | $ 3,897 |
| Acquisitions | — | — | 25 | 25 |
| Balance at September 30, 2019 | $ 1,535 | $ 261 | $ 2,126 | $ 3,922 |

The following table presents details of our other intangible assets included in other long-term assets in the accompanying condensed consolidated balance sheets at September 30, 2019 and December 31, 2018.

| | | September 30, 2019 | | | December 31, 2018 | | |
|---|---|---|---|---|---|---|---|
| | Weighted Average Life | Cost | Accumulated Amortization | Net | Cost | Accumulated Amortization | Net |
| | | ($ in millions) | | | | | |
| Other intangible assets: | | | | | | | |
| Customer contracts/ relationships | 8.7 years | $ 647 | $ 481 | $ 166 | $ 646 | $ 434 | $ 212 |
| Trade names and technology | 6.4 years | 84 | 84 | — | 84 | 83 | 1 |
| Provider contracts | 11.8 years | 69 | 42 | 27 | 68 | 37 | 31 |
| Noncompetes and other | 7.3 years | 29 | 28 | 1 | 29 | 28 | 1 |
| Total other intangible assets | 8.7 years | $ 829 | $ 635 | $ 194 | $ 827 | $ 582 | $ 245 |

Amortization expense for other intangible assets was approximately $17 million for the three months ended September 30, 2019 and $19 million for the three months ended September 30, 2018. For the nine months ended September 30, 2019 and 2018, amortization expense for other intangible assets was approximately $53 million and $70 million, respectively. Amortization expense for the nine months ended September 30, 2018 included $12 million associated with the write-off of a trade name value reflecting the re-branding of certain provider assets. The following table presents our estimate of amortization expense remaining for 2019 and each of the five next succeeding years:

| | (in millions) |
|---|---|
| For the years ending December 31, | |
| 2019 | $ 17 |
| 2020 | 67 |
| 2021 | 34 |
| 2022 | 31 |
| 2023 | 18 |
| 2024 | 11 |

## 8. LEASES

***2019***

We determine if a contract contains a lease by evaluating the nature and substance of the agreement. We lease facilities, computer hardware, and other furniture and equipment. Leases with an initial term of 12 months or less are not recorded on the balance sheet; we recognize lease expense for these leases on a straight-line basis over the lease term. For new lease agreements, we combine lease and nonlease components for all of our asset classes. See Note 2 for further information.

When portions of the lease payments are not fixed or depend on an index or rate, we consider those payments to be variable in nature. These include, but are not limited to, common area maintenance, taxes and insurance. Variable lease payments are recorded in the period in which the obligation for the payment is incurred.

Most leases include options to renew, with renewal terms that can extend the lease term. The exercise of lease renewal options is at our sole discretion. Certain leases also include options to purchase the leased property. The depreciable life of assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise. Our lease agreements do not contain any material residual value guarantees or material restrictive covenants.

At September 30, 2019, $404 million of operating ROU assets are included within other long-term assets in our condensed consolidated balance sheet. Additionally, at September 30, 2019, $120 million and $324 million of operating ROU lease liabilities are included within trade accounts payable and accrued expenses and other long-term liabilities, respectively, in our condensed consolidated balance sheet based on the remaining lease term.

For the three and nine months ended September 30, 2019, total fixed operating lease costs, excluding short-term lease costs, were $37 million and $115 million, respectively, and are included within operating costs in our condensed consolidated statement of income. Short-term lease costs were not material. In addition, for the three and nine months ended September 30, 2019, total variable operating lease costs were $21 million and $56 million, respectively and are included within operating costs in our condensed consolidated statement of income. We sublease facilities or partial facilities to third party tenants for space not used in our operations. For the three and nine months ended September 30, 2019, sublease rental income was $10 million and $29 million, respectively, and is included within operating costs in our condensed consolidated statement of income.

The weighted average remaining lease term is 4.8 years with a weighted average discount rate of 4.2% at September 30, 2019. For the nine months ended September 30, 2019, cash paid for amounts included in the measurement of lease liabilities included within our operating cash flows was $112 million.

| **Maturity of Lease Liabilities** | | **September 30, 2019** |
|---|---|---|
| | | **(in millions)** |
| 2019 (excluding the nine months ended September 30, 2019) | $ | 36 |
| 2020 | | 128 |
| 2021 | | 110 |
| 2022 | | 89 |
| 2023 | | 45 |
| After 2023 | | 82 |
| Total lease payments | | 490 |
| Less: Interest | | 46 |
| Present value of ROU lease liabilities | $ | 444 |

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As most of our leases do not provide an implicit rate, we use our incremental borrowing rate, as adjusted for collateralized borrowings, based on the information available at date of adoption or commencement date in determining the present value of lease payments.

***For the year ended 2018, under prior lease disclosure requirements***

We lease facilities, computer hardware, and other furniture and equipment under long-term operating leases that are non-cancelable and expire on various dates through 2046. We sublease facilities or partial facilities to third party tenants for space not used in our operations. Rent with scheduled escalation terms are accounted for on a straight-line basis over the lease term. Rent expense and sublease rental income, which are recorded net as an operating cost, for all operating leases were as follows for the years ended December 31, 2018, 2017 and 2016:

| | 2018 | 2017 | 2016 |
|---|---|---|---|
| | | (in millions) | |
| Rent expense | $ 167 | $ 204 | $ 179 |
| Sublease rental income | (32) | (33) | (26) |
| Net rent expense | $ 135 | $ 171 | $ 153 |

Future annual minimum payments due subsequent to December 31, 2018 under all of our noncancelable operating leases with initial terms in excess of one year are as follows:

| | Minimum Lease Payments | Sublease Rental Receipts | Net Lease Commitments |
|---|---|---|---|
| | | (in millions) | |
| For the years ending December 31,: | | | |
| 2019 | $ 147 | $ (13) | $ 134 |
| 2020 | 113 | (12) | 101 |
| 2021 | 96 | (10) | 86 |
| 2022 | 79 | (9) | 70 |
| 2023 | 34 | (9) | 25 |
| Thereafter | 50 | (23) | 27 |
| Total | $ 519 | $ (76) | $ 443 |

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(Unaudited)

## 9. BENEFITS PAYABLE

On a consolidated basis, activity in benefits payable, was as follows for the nine months ended September 30, 2019 and 2018:

| | For the nine months ended September 30, | |
|---|---|---|
| | 2019 | 2018 |
| | (in millions) | |
| Balances, beginning of period | $ 4,862 | $ 4,668 |
| Less: Reinsurance recoverables | (95) | (70) |
| Balances, beginning of period, net | 4,767 | 4,598 |
| Incurred related to: | | |
| Current year | 40,499 | 34,915 |
| Prior years | (331) | (467) |
| Total incurred | 40,168 | 34,448 |
| Paid related to: | | |
| Current year | (34,625) | (30,204) |
| Prior years | (4,158) | (3,920) |
| Total paid | (38,783) | (34,124) |
| Reinsurance recoverable | 68 | 98 |
| Balances, end of period | $ 6,220 | $ 5,020 |

Amounts incurred related to prior periods vary from previously estimated liabilities as the claims ultimately are settled. Negative amounts reported for incurred related to prior years result from claims being ultimately settled for amounts less than originally estimated (favorable development).

Our reserving practice is to consistently recognize the actuarial best estimate of our ultimate liability for claims. Actuarial standards require the use of assumptions based on moderately adverse experience, which generally results in favorable reserve development, or reserves that are considered redundant.

Benefits expense excluded from the previous table related to our long duration policies was as follows for the nine months ended September 30, 2019 and 2018. The Other Businesses category was related to our closed-block of commercial long-term care insurance policies, which were sold in 2018. We also exited our Individual Commercial business beginning January 1, 2018.

| | For the nine months ended September 30, | |
|---|---|---|
| | 2019 | 2018 |
| | (in millions) | |
| Future policy benefits: | | |
| Individual Commercial | $ — | $ (14) |
| Other Businesses | — | 15 |
| Total future policy benefits | $ — | $ 1 |

***Incurred and Paid Claims Development***

The following discussion provides information about incurred and paid claims development for our Retail and Group and Specialty segments as of September 30, 2019 and 2018, net of reinsurance, and the total estimate of benefits payable for claims incurred but not reported, or IBNR, included within the net incurred claims amounts. Our Individual Commercial segment incurred claims development was favorable by $58 million for the nine months ended September 30, 2018.

*Retail Segment*

Activity in benefits payable for our Retail segment was as follows for the nine months ended September 30, 2019 and 2018:

| | For the nine months ended September 30, | |
|---|---|---|
| | 2019 | 2018 |
| | (in millions) | |
| Balances, beginning of period | $ 4,338 | $ 3,963 |
| Less: Reinsurance recoverables | (95) | (70) |
| Balances, beginning of period, net | 4,243 | 3,893 |
| Incurred related to: | | |
| Current year | 36,762 | 31,209 |
| Prior years | (366) | (367) |
| Total incurred | 36,396 | 30,842 |
| Paid related to: | | |
| Current year | (31,476) | (27,062) |
| Prior years | (3,634) | (3,334) |
| Total paid | (35,110) | (30,396) |
| Reinsurance recoverable | 68 | 98 |
| Balances, end of period | $ 5,597 | $ 4,437 |

At September 30, 2019, benefits payable for our Retail segment included IBNR of approximately $3.5 billion, primarily associated with claims incurred in 2019.

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**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**
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*Group and Specialty Segment*

Activity in benefits payable for our Group and Specialty segment, was as follows for the nine months ended September 30, 2019 and 2018:

| | For the nine months ended September 30, | |
|---|---|---|
| | 2019 | 2018 |
| | (in millions) | |
| Balances, beginning of period | $ 517 | $ 568 |
| Incurred related to: | | |
| Current year | 4,142 | 4,018 |
| Prior years | 35 | (41) |
| Total incurred | 4,177 | 3,977 |
| Paid related to: | | |
| Current year | (3,547) | (3,462) |
| Prior years | (524) | (509) |
| Total paid | (4,071) | (3,971) |
| Balances, end of period | $ 623 | $ 574 |

At September 30, 2019, benefits payable for our Group and Specialty segment included IBNR of approximately $530 million, primarily associated with claims incurred in 2019.

*Reconciliation to Consolidated*

The reconciliation of the net incurred and paid claims development tables to benefits payable in the consolidated statement of financial position is as follows:

**Reconciliation of the Disclosure of Incurred and Paid Claims Development to Benefits Payable, net of reinsurance**

| | September 30, 2019 |
|---|---|
| Net outstanding liabilities | (in millions) |
| Retail | $ 5,529 |
| Group and Specialty | 623 |
| Benefits payable, net of reinsurance | 6,152 |
| | |
| Reinsurance recoverable on unpaid claims | |
| Retail | 68 |
| Total benefits payable, gross | $ 6,220 |

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## 10. EARNINGS PER COMMON SHARE COMPUTATION

Detail supporting the computation of basic and diluted earnings per common share was as follows for the three and nine months ended September 30, 2019 and 2018:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2019 | 2018 | 2019 | 2018 |
| | (dollars in millions, except per common share results; number of shares in thousands) | | | |
| Net income available for common stockholders | $ 689 | $ 644 | $ 2,195 | $ 1,328 |
| Weighted average outstanding shares of common stock used to compute basic earnings per common share | 133,321 | 137,709 | 134,589 | 137,792 |
| Dilutive effect of: | | | | |
| Employee stock options | 101 | 186 | 99 | 199 |
| Restricted stock | 603 | 783 | 501 | 704 |
| Shares used to compute diluted earnings per common share | 134,025 | 138,678 | 135,189 | 138,695 |
| Basic earnings per common share | $ 5.16 | $ 4.68 | $ 16.31 | $ 9.64 |
| Diluted earnings per common share | $ 5.14 | $ 4.65 | $ 16.24 | $ 9.58 |
| Number of antidilutive stock options and restricted stock excluded from computation | 302 | 36 | 589 | 284 |

## 11. STOCKHOLDERS' EQUITY

***Dividends***

The following table provides details of dividend payments, excluding dividend equivalent rights for unvested stock awards, in 2018 and 2019 under our Board approved quarterly cash dividend policy:

| Record Date | Payment Date | Amount per Share | Total Amount |
|---|---|---|---|
| | | | (in millions) |
| **2018 payments** | | | |
| 12/29/2017 | 1/26/2018 | $ 0.40 | $ 55 |
| 3/30/2018 | 4/27/2018 | $ 0.50 | $ 69 |
| 6/29/2018 | 7/27/2018 | $ 0.50 | $ 69 |
| 9/28/2018 | 10/26/2018 | $ 0.50 | $ 69 |
| **2019 payments** | | | |
| 12/31/2018 | 1/25/2019 | $ 0.50 | $ 68 |
| 3/29/2019 | 4/26/2019 | $ 0.55 | $ 74 |
| 6/28/2019 | 7/26/2019 | $ 0.55 | $ 74 |
| 9/30/2019 | 10/25/2019 | $ 0.55 | $ 73 |

On October 24, 2019, the Board declared a cash dividend of $0.55 per share payable on January 31, 2020, to stockholders of record on December 31, 2019.

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***Stock Repurchases***

Our Board of Directors may authorize the purchase of our common stock shares. Under the share repurchase authorization, shares may be purchased from time to time at prevailing prices in the open market, by block purchases, through plans designed to comply with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended, or in privately-negotiated transactions, including pursuant to accelerated share repurchase agreements with investment banks, subject to certain regulatory restrictions on volume, pricing, and timing.

On December 14, 2017, our Board of Directors authorized the repurchase of up to $3.0 billion of our common shares expiring on December 31, 2020, exclusive of shares repurchased in connection with employee stock plans.

On November 28, 2018, we entered into an accelerated stock repurchase agreement, the November 2018 ASR, with Goldman Sachs to repurchase $750 million of our common stock as part of the $3.0 billion share repurchase program authorized by the Board of Directors on December 14, 2017. On November 29, 2018, we made a payment of $750 million to Goldman Sachs from available cash on hand and received an initial delivery of 1.94 million shares of our common stock from Goldman Sachs based on the then current price of our common stock. The payment to Goldman Sachs was recorded as a reduction to stockholders' equity, consisting of a $600 million increase in treasury stock, which reflects the value of the initial 1.94 million shares received upon initial settlement, and a $150 million decrease in capital in excess of par value, which reflected the value of stock held back by Goldman Sachs pending final settlement of the November 2018 ASR. Upon final settlement of the November 2018 ASR on February 28, 2019, we received an additional 0.6 million shares as determined by the average daily volume weighted-averages share price of our common stock during the term of the agreement of $295.15, less a discount and subject to adjustments pursuant to the terms and conditions of the November 2018 ASR, bringing the total shares received under this program to 2.54 million. In addition, upon settlement we reclassified the $150 million value of stock initially held back by Goldman Sachs from capital in excess of par value to treasury stock.

On July 30, 2019, the Board of Directors replaced a previous share repurchase authorization of up to $3 billion (of which approximately $1.03 billion remained unused) with a new authorization for repurchases of up to $3 billion of our common shares exclusive of shares repurchased in connection with employee stock plans, expiring on June 30, 2022.

On July 31, 2019, we entered into an accelerated stock repurchase agreement, the July 2019 ASR, with Citibank, N.A., or Citi, to repurchase $1 billion of our common stock. On August 2, 2019, we made a payment of $1 billion to Citi and received an initial delivery of 2.7 million shares of our common stock. We recorded the payment to Citi as a reduction to stockholders' equity, consisting of an $800 million increase in treasury stock, which reflects the value of the initial 2.7 million shares received upon initial settlement, and a $200 million decrease in capital in excess of par value, which reflects the value of stock held back by Citi pending final settlement of the July 2019 ASR. The final number of shares that we may receive, or be required to remit, under the agreement, will be determined based on the daily volume-weighted average share price of our common stock over the term of the agreement, less a discount and subject to adjustments pursuant to the terms and conditions of the July 2019 ASR. We expect final settlement under the July 2019 ASR to occur during the fourth quarter of 2019. The agreement contains provisions customary for agreements of this type, including provisions for adjustments to the transaction terms upon certain specified events, the circumstances generally under which final settlement of the agreement may be accelerated, extended, or terminated early by Citi or Humana as well as various acknowledgments and representations made by the parties to each other. At final settlement, under certain circumstances, we may be entitled to receive additional shares of our common stock from Citi or we may be required to make a payment. If we are obligated to make payment, we may elect to satisfy such obligation in cash or shares of our common stock.

In connection with employee stock plans, we acquired 35,000 common shares for $10 million and 0.3 million common shares for $70 million during the nine months ended September 30, 2019 and 2018, respectively.

***Treasury Stock Reissuance***

We reissued 0.2 million shares of treasury stock during the nine months ended September 30, 2019 at a cost of $18.6 million associated with restricted stock unit vestings and option exercises.

***Accumulated Other Comprehensive Income***

Accumulated other comprehensive income included net unrealized gains, net of tax, on our investment securities of $177 million at September 30, 2019 and net unrealized losses, net of tax, on our investment securities of $159 million at December 31, 2018.

## 12. INCOME TAXES

The effective income tax rate was 22.5% and 23.8% for the three and nine months ended September 30, 2019, respectively, compared to 29.1% and 18.8% for the three and nine months ended September 30, 2018, respectively, primarily due to the impact of the suspension of the non-deductible health insurance industry fee in 2019 as well as the deferred tax benefit recognized in 2018 from the loss on sale of KMG. The effective income tax rate for the nine months ended September 30, 2018 reflected a $430 million deferred tax benefit, resulting from the loss on the sale of KMG attributable to its original tax basis and subsequent capital contributions to fund accumulated losses.

## 13. DEBT

The carrying value of debt outstanding, net of unamortized debt issuance costs, was as follows at September 30, 2019 and December 31, 2018:

| | September 30, 2019 | December 31, 2018 |
|---|---|---|
| | (in millions) | |
| Short-term debt: | | |
| Commercial paper | $ 299 | $ 645 |
| Term note | — | 650 |
| Senior note: | | |
| $400 million, 2.625% due October 1, 2019 | 400 | 399 |
| Total short-term debt | $ 699 | $ 1,694 |
| | | |
| Long-term debt: | | |
| Senior notes: | | |
| $400 million, 2.50% due December 15, 2020 | $ 399 | $ 398 |
| $400 million, 2.90% due December 15, 2022 | 397 | 396 |
| $600 million, 3.15% due December 1, 2022 | 597 | 596 |
| $600 million, 3.85% due October 1, 2024 | 597 | 597 |
| $600 million, 3.95% due March 15, 2027 | 595 | 594 |
| $500 million, 3.125% due August 15, 2029 | 495 | — |
| $250 million, 8.15% due June 15, 2038 | 262 | 263 |
| $400 million, 4.625% due December 1, 2042 | 396 | 396 |
| $750 million, 4.95% due October 1, 2044 | 739 | 739 |
| $400 million, 4.80% due March 15, 2047 | 396 | 396 |
| $500 million, 3.95% due August 15, 2049 | 492 | — |
| Total long-term debt | $ 5,365 | $ 4,375 |

***Senior Notes***

In August 2019, we issued $500 million of 3.125% senior notes due August 15, 2029 and $500 million of 3.950% senior notes due August 15, 2049. Our net proceeds, reduced for the underwriters' discount and commission and offering expenses paid as of September 30, 2019 were $987 million. We used the net proceeds from this offering, together with available cash, to repay the $650 million outstanding amount due under our term note in August 2019, and the $400 million aggregate principal amount of our 2.625% senior notes due on its maturity date of October 1, 2019.

Our senior notes, which are unsecured, may be redeemed at our option at any time at 100% of the principal amount plus accrued interest and a specified make-whole amount. The 8.15% senior notes are subject to an interest rate adjustment if the debt ratings assigned to the notes are downgraded (or subsequently upgraded). In addition, our senior notes contain a change of control provision that may require us to purchase the notes under certain circumstances.

***Credit Agreement***

Our 5-year, $2.0 billion unsecured revolving credit agreement expires May 2022. Under the credit agreement, at our option, we can borrow on either a competitive advance basis or a revolving credit basis. The revolving credit portion bears interest at either LIBOR plus a spread or the base rate plus a spread. The LIBOR spread, currently 110.0 basis points, varies depending on our credit ratings ranging from 91.0 to 150.0 basis points. We also pay an annual facility fee regardless of utilization. This facility fee, currently 15.0 basis points, may fluctuate between 9.0 and 25.0 basis points, depending upon our credit ratings. The competitive advance portion of any borrowings will bear interest at market rates prevailing at the time of borrowing on either a fixed rate or a floating rate based on LIBOR, at our option.

The terms of the credit agreement include standard provisions related to conditions of borrowing which could limit our ability to borrow additional funds. In addition, the credit agreement contains customary restrictive covenants and a financial covenant regarding maximum debt to capitalization of 50%, as well as customary events of default. We are in compliance with this financial covenant, with actual debt to capitalization of 34% as measured in accordance with the credit agreement as of September 30, 2019. Upon our agreement with one or more financial institutions, we may expand the aggregate commitments under the credit agreement to a maximum of $2.5 billion, through a $500 million incremental loan facility.

At September 30, 2019, we had no borrowings and no letters of credit outstanding under the credit agreement. Accordingly, as of September 30, 2019, we had $2.0 billion of remaining borrowing capacity (which excludes the uncommitted $500 million incremental loan facility under the credit agreement), none of which would be restricted by our financial covenant compliance requirement. We have other customary, arms-length relationships, including financial advisory and banking, with some parties to the credit agreement.

***Commercial Paper***

Under our commercial paper program we may issue short-term, unsecured commercial paper notes privately placed on a discount basis through certain broker dealers at any time not to exceed $2 billion. Amounts available under the program may be borrowed, repaid and re-borrowed from time to time. The net proceeds of issuances have been and are expected to be used for general corporate purposes. The maximum principal amount outstanding at any one time during the nine months ended September 30, 2019 was $670 million, with $299 million outstanding at September 30, 2019 compared to $645 million outstanding at December 31, 2018. The outstanding commercial paper at September 30, 2019 had a weighted average annual interest rate of 2.5%.

***Term Note***

In November 2018, we entered into a $1.0 billion term note agreement with a bank at a variable rate of interest due within one year. We may elect to incur interest at either the bank's base rate or LIBOR plus 115 basis points. The base rate is defined as the higher of the daily federal funds rate plus 50 basis points; or the bank's prime rate; or LIBOR plus 100 basis points. The term note shares the customary terms and provisions as well as financial covenants of our

Credit Agreement, as discussed above. The note was prepayable without penalty. We repaid $350 million prior to December 31, 2018 and repaid the outstanding balance of $650 million in August 2019.

## 14. COMMITMENTS, GUARANTEES AND CONTINGENCIES

***Government Contracts***

Our Medicare products, which accounted for approximately 80% of our total premiums and services revenue for the nine months ended September 30, 2019, primarily consisted of products covered under the Medicare Advantage and Medicare Part D Prescription Drug Plan contracts with the federal government. These contracts are renewed generally for a calendar year term unless CMS notifies us of its decision not to renew by May 1 of the calendar year in which the contract would end, or we notify CMS of our decision not to renew by the first Monday in June of the calendar year in which the contract would end. All material contracts between Humana and CMS relating to our Medicare products have been renewed for 2020, and all of our product offerings for 2020 have been approved.

CMS uses a risk-adjustment model which adjusts premiums paid to Medicare Advantage, or MA, plans according to health status of covered members. The risk-adjustment model, which CMS implemented pursuant to the Balanced Budget Act of 1997 (BBA) and the Benefits Improvement and Protection Act of 2000 (BIPA), generally pays more where a plan's membership has higher expected costs. Under this model, rates paid to MA plans are based on actuarially determined bids, which include a process whereby our prospective payments are based on our estimated cost of providing standard Medicare-covered benefits to an enrollee with a "national average risk profile." That baseline payment amount is adjusted to reflect the health status of our enrolled membership. Under the risk-adjustment methodology, all MA plans must collect and submit the necessary diagnosis code information from hospital inpatient, hospital outpatient, and physician providers to CMS within prescribed deadlines. The CMS risk-adjustment model uses the diagnosis data to calculate the risk-adjusted premium payment to MA plans, which CMS adjusts for coding pattern differences between the health plans and the government fee-for-service program. We generally rely on providers, including certain providers in our network who are our employees, to code their claim submissions with appropriate diagnoses, which we send to CMS as the basis for our payment received from CMS under the actuarial risk-adjustment model. We also rely on these providers to document appropriately all medical data, including the diagnosis data submitted with claims. In addition, we conduct medical record reviews as part of our data and payment accuracy compliance efforts, to more accurately reflect diagnosis conditions under the risk adjustment model. These compliance efforts include the internal contract level audits described in more detail below, as well as ordinary course reviews of our internal business processes.

CMS is phasing-in the process of calculating risk scores using diagnoses data from the Risk Adjustment Processing System, or RAPS, to diagnoses data from the Encounter Data System, or EDS. The RAPS process requires MA plans to apply a filter logic based on CMS guidelines and only submit diagnoses that satisfy those guidelines. For submissions through EDS, CMS requires MA plans to submit all the encounter data and CMS will apply the risk adjustment filtering logic to determine the risk scores. For 2018, 15% of the risk score was calculated from claims data submitted through EDS. In 2019 and 2020 CMS will increase that percentage to 25% and 50%, respectively. The phase-in from RAPS to EDS could result in different risk scores from each dataset as a result of plan processing issues, CMS processing issues, or filtering logic differences between RAPS and EDS, and could have a material adverse effect on our results of operations, financial position, or cash flows.

CMS and the Office of the Inspector General of Health and Human Services, or HHS-OIG, are continuing to perform audits of various companies’ selected MA contracts related to this risk adjustment diagnosis data. We refer to these audits as Risk-Adjustment Data Validation Audits, or RADV audits. RADV audits review medical records in an attempt to validate provider medical record documentation and coding practices which influence the calculation of premium payments to MA plans.

In 2012, CMS released a “Notice of Final Payment Error Calculation Methodology for Part C Medicare Advantage Risk Adjustment Data Validation (RADV) Contract-Level Audits.” The payment error calculation methodology provided that, in calculating the economic impact of audit results for an MA contract, if any, the results of the RADV audit sample would be extrapolated to the entire MA contract after a comparison of the audit results to a similar audit of the government’s traditional fee-for-service Medicare program, or Medicare FFS. We refer to the process of accounting for errors in FFS claims as the "FFS Adjuster." This comparison of RADV audit results to the FFS error rate is necessary to determine the economic impact, if any, of RADV audit results because the government used the Medicare FFS program data set, including any attendant errors that are present in that data set, to estimate the costs of various health status conditions and to set the resulting adjustments to MA plans' payment rates in order to establish actuarial equivalence in payment rates as required under the Medicare statute. CMS already makes other adjustments to payment rates based on a comparison of coding pattern differences between MA plans and Medicare FFS data (such as for frequency of coding for certain diagnoses in MA plan data versus the Medicare FFS program dataset).

The final RADV extrapolation methodology, including the first application of extrapolated audit results to determine audit settlements, is expected to be applied to CMS RADV contract level audits conducted for contract year 2011 and subsequent years. CMS is currently conducting RADV contract level audits for certain of our Medicare Advantage plans.

Estimated audit settlements are recorded as a reduction of premiums revenue in our consolidated statements of income, based upon available information. We perform internal contract level audits based on the RADV audit methodology prescribed by CMS. Included in these internal contract level audits is an audit of our Private Fee-For Service business which we used to represent a proxy of the FFS Adjuster which has not yet been finalized. We based our accrual of estimated audit settlements for each contract year on the results of these internal contract level audits and update our estimates as each audit is completed. Estimates derived from these results were not material to our results of operations, financial position, or cash flows. We report the results of these internal contract level audits to CMS, including identified overpayments, if any.

On October 26, 2018, CMS issued a proposed rule and accompanying materials (which we refer to as the “Proposed Rule”) related to, among other things, the RADV audit methodology described above. If implemented, the Proposed Rule would use extrapolation in RADV audits applicable to payment year 2011 contract-level audits and all subsequent audits, without the application of a FFS Adjuster to audit findings. We believe that the Proposed Rule fails to address adequately the statutory requirement of actuarial equivalence, and have provided substantive comments to CMS on the Proposed Rule as part of the notice-and-comment rulemaking process. Whether, and to what extent, CMS finalizes the Proposed Rule, and any related regulatory, industry or company reactions, could have a material adverse effect on our results of operations, financial position, or cash flows.

In addition, as part of our internal compliance efforts, we routinely perform ordinary course reviews of our internal business processes related to, among other things, our risk coding and data submissions in connection with the risk- adjustment model. These reviews may also result in the identification of errors and the submission of corrections to CMS, that may, either individually or in the aggregate, be material. As such, the result of these reviews may have a material adverse effect on our results of operations, financial position, or cash flows.

We believe that CMS' statements and policies regarding the requirement to report and return identified overpayments received by MA plans are inconsistent with CMS' 2012 RADV audit methodology, and the Medicare statute's requirements. These statements and policies, such as certain statements contained in the preamble to CMS' final rule release regarding Medicare Advantage and Part D prescription drug benefit program regulations for Contract Year 2015 (which we refer to as the "Overpayment Rule"), and the Proposed Rule, appear to equate each Medicare Advantage risk adjustment data error with an “overpayment” without addressing the principles underlying the FFS Adjuster referenced above. On September 7, 2018, the Federal District Court for the District of Columbia vacated CMS's Overpayment Rule, concluding that it violated the Medicare statute, including the requirement for actuarial equivalence, and that the Overpayment Rule was also arbitrary and capricious in departing from CMS's RADV methodology without adequate explanation (among other reasons). CMS has filed a motion for reconsideration related to certain aspects of the Federal District Court's opinion and has simultaneously filed a notice to appeal the decision to the Circuit Court of Appeals.

We will continue to work with CMS to ensure that MA plans are paid accurately and that payment model principles are in accordance with the requirements of the Social Security Act, which, if not implemented correctly could have a material adverse effect on our results of operations, financial position, or cash flows.

At September 30, 2019, our military services business, which accounted for approximately 1% of our total premiums and services revenue for the nine months ended September 30, 2019, primarily consisted of the TRICARE T2017 East Region contract. The T2017 East Region contract is a consolidation of the former T3 North and South Regions, comprising thirty-two states and approximately 6 million TRICARE beneficiaries, under which delivery of health care services commenced on January 1, 2018. The T2017 East Region contract is a 5-year contract set to expire on December 31, 2022 and is subject to renewals on January 1 of each year during its term at the government's option.

Our state-based Medicaid business accounted for approximately 4% of our total premiums and services revenue for the nine months ended September 30, 2019. In addition to our state-based Temporary Assistance for Needy Families, or TANF, Medicaid contracts in Florida and Kentucky, we have contracts in Florida for Long Term Support Services (LTSS), and in Illinois for stand-alone dual eligible demonstration programs serving individuals dually eligible for both the federal Medicare program and the applicable state-based Medicaid program.

The loss of any of the contracts above or significant changes in these programs as a result of legislative or regulatory action, including reductions in premium payments to us, regulatory restrictions on profitability, including reviews by regulatory bodies that may compare our Medicare Advantage profitability to our non-Medicare Advantage business profitability, or compare the profitability of various products within our Medicare Advantage business, and require that they remain within certain ranges of each other, or increases in member benefits or member eligibility criteria without corresponding increases in premium payments to us, may have a material adverse effect on our results of operations, financial position, and cash flows.

***Legal Proceedings and Certain Regulatory Matters***

As previously disclosed, the Civil Division of the United States Department of Justice provided us with an information request in December 2014, concerning our Medicare Part C risk adjustment practices. The request relates to our oversight and submission of risk adjustment data generated by providers in our Medicare Advantage network, as well as to our business and compliance practices related to risk adjustment data generated by our providers and by us, including medical record reviews conducted as part of our data and payment accuracy compliance efforts, the use of health and well-being assessments, and our fraud detection efforts. We believe that this request for information is in connection with a wider review of Medicare Risk Adjustment generally that includes a number of Medicare Advantage plans, providers and vendors. We continue to cooperate with and voluntarily respond to the information requests from the Department of Justice. These matters are expected to result in additional qui tam litigation.

As previously disclosed, on January 19, 2016, an individual filed a qui tam suit captioned *United States of America ex rel. Steven Scott v. Humana, Inc.*, in United States District Court, Central District of California, Western Division. The complaint alleges certain civil violations by us in connection with the actuarial equivalence of the plan benefits under Humana's Basic PDP plan, a prescription drug plan offered by us under Medicare Part D. The action seeks damages and penalties on behalf of the United States under the False Claims Act. The court ordered the qui tam action unsealed on September 13, 2017, so that the relator could proceed, following notice from the U.S. Government that it was not intervening at that time. On January 29, 2018, the suit was transferred to the United States District Court, Western District of Kentucky, Louisville Division. We take seriously our obligations to comply with applicable CMS requirements and actuarial standards of practice, and continue to vigorously defend against these allegations since the transfer to the Western District of Kentucky. We have engaged in active discovery with the relator who has pursued the matter on behalf of the United States following its unsealing, and expect that discovery process to conclude in the near future and for the Court to consider our motion for summary judgment.

On November 2, 2017, we filed suit against the United States of America in the United States Court of Federal Claims, on behalf of our health plans seeking recovery from the federal government of approximately $611 million in payments under the risk corridor premium stabilization program established under Health Care Reform, for years 2014, 2015 and 2016. Our case has been stayed by the Court, pending resolution of similar cases filed by other insurers. We have not recognized revenue, nor have we recorded a receivable, for any amount due from the federal government for unpaid risk corridor payments as of September 30, 2019. We have fully recognized all liabilities due to the federal government that we have incurred under the risk corridor program, and have paid all amounts due to the federal government as required. There is no assurance that we will prevail in the lawsuit.

*Other Lawsuits and Regulatory Matters*

Our current and past business practices are subject to review or other investigations by various state insurance and health care regulatory authorities and other state and federal regulatory authorities. These authorities regularly scrutinize the business practices of health insurance, health care delivery and benefits companies. These reviews focus on numerous facets of our business, including claims payment practices, statutory capital requirements, provider contracting, risk adjustment, competitive practices, commission payments, privacy issues, utilization management practices, pharmacy benefits, access to care, and sales practices, among others. Some of these reviews have historically resulted in fines imposed on us and some have required changes to some of our practices. We continue to be subject to these reviews, which could result in additional fines or other sanctions being imposed on us or additional changes in some of our practices.

We also are involved in various other lawsuits that arise, for the most part, in the ordinary course of our business operations, certain of which may be styled as class-action lawsuits. Among other matters, this litigation may include employment matters, claims of medical malpractice, bad faith, nonacceptance or termination of providers, anticompetitive practices, improper rate setting, provider contract rate and payment disputes, including disputes over reimbursement rates required by statute, general contractual matters, intellectual property matters, and challenges to subrogation practices. Under state guaranty assessment laws, including those related to state cooperative failures in the industry, we may be assessed (up to prescribed limits) for certain obligations to the policyholders and claimants of insolvent insurance companies that write the same line or lines of business as we do.

As a government contractor, we may also be subject to qui tam litigation brought by individuals who seek to sue on behalf of the government, alleging that the government contractor submitted false claims to the government including, among other allegations, those resulting from coding and review practices under the Medicare risk adjustment model. Qui tam litigation is filed under seal to allow the government an opportunity to investigate and to decide if it wishes to intervene and assume control of the litigation. If the government does not intervene, the individual may continue to prosecute the action on his or her own, on behalf of the government. We also are subject to other allegations of non-performance of contractual obligations to providers, members, and others, including failure to properly pay claims, improper policy terminations, challenges to our implementation of the Medicare Part D prescription drug program and other litigation.

A limited number of the claims asserted against us are subject to insurance coverage. Personal injury claims, claims for extra contractual damages, care delivery malpractice, and claims arising from medical benefit denials are covered by insurance from our wholly owned captive insurance subsidiary and excess carriers, except to the extent that claimants seek punitive damages, which may not be covered by insurance in certain states in which insurance coverage for punitive damages is not permitted. In addition, insurance coverage for all or certain forms of liability has become increasingly costly and may become unavailable or prohibitively expensive in the future.

We record accruals for the contingencies discussed in the sections above to the extent that we conclude it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. No estimate of the possible loss or range of loss in excess of amounts accrued, if any, can be made at this time regarding the matters specifically described above because of the inherently unpredictable nature of legal proceedings, which also may be exacerbated by various factors, including: (i) the damages sought in the proceedings are unsubstantiated or indeterminate; (ii) discovery is not complete; (iii) the proceeding is in its early stages; (iv) the matters present legal uncertainties; (v) there are significant facts in dispute; (vi) there are a large number of parties (including where it is uncertain how liability, if any, will be shared among multiple defendants); or (vii) there is a wide range of potential outcomes.

The outcome of any current or future litigation or governmental or internal investigations, including the matters described above, cannot be accurately predicted, nor can we predict any resulting judgments, penalties, fines or other sanctions that may be imposed at the discretion of federal or state regulatory authorities or as a result of actions by third parties. Nevertheless, it is reasonably possible that any such outcome of litigation, judgments, penalties, fines or other sanctions could be substantial, and the outcome of these matters may have a material adverse effect on our results of operations, financial position, and cash flows, and may also affect our reputation.

## 15. SEGMENT INFORMATION

We manage our business with three reportable segments: Retail, Group and Specialty, and Healthcare Services. Beginning January 1, 2018, we exited the individual commercial fully-insured medical health insurance business, as well as certain other business, and therefore no longer report separately the Individual Commercial segment and the Other Business category in the current year. Previously, the Other Business category included businesses that were not individually reportable because they did not meet the quantitative thresholds required by generally accepted accounting principles, primarily our closed-block of commercial long-term care insurance policies which were sold in 2018. The reportable segments are based on a combination of the type of health plan customer and adjacent businesses centered on well-being solutions for our health plans and other customers, as described below. These segment groupings are consistent with information used by our Chief Executive Officer, the Chief Operating Decision Maker, to assess performance and allocate resources.

The Retail segment consists of Medicare benefits, marketed to individuals or directly via group Medicare accounts. In addition, the Retail segment also includes our contract with CMS to administer the Limited Income Newly Eligible Transition, or LI-NET, prescription drug plan program and contracts with various states to provide Medicaid, dual eligible, and Long-Term Support Services benefits, which we refer to collectively as our state-based contracts. The Group and Specialty segment consists of employer group commercial fully-insured medical and specialty health insurance benefits marketed to individuals and employer groups, including dental, vision, and other supplemental health benefits, as well as administrative services only, or ASO products. In addition, our Group and Specialty segment includes our military services business, primarily our TRICARE T2017 East Region contract. The Healthcare Services segment includes our services offered to our health plan members as well as to third parties, including pharmacy solutions, provider services, and clinical care service, such as home health and other services and capabilities to promote wellness and advance population health, including our minority investment in Kindred at Home. We reported under the category of Other Businesses those businesses that did not align with the reportable segments described above, primarily our closed-block long-term care insurance policies, which were sold in 2018.

Our Healthcare Services intersegment revenues primarily relate to managing prescription drug coverage for members of our other segments through Humana Pharmacy Solutions®, or HPS, and includes the operations of Humana Pharmacy, Inc., our mail order pharmacy business. These revenues consist of the prescription price (ingredient cost plus dispensing fee), including the portion to be settled with the member (co-share) or with the government (subsidies), plus any associated administrative fees. Services revenues related to the distribution of prescriptions by third party retail pharmacies in our networks are recognized when the claim is processed and product revenues from dispensing prescriptions from our mail order pharmacies are recorded when the prescription or product is shipped. Our pharmacy operations, which are responsible for designing pharmacy benefits, including defining member co-share responsibilities, determining formulary listings, contracting with retail pharmacies, confirming member eligibility, reviewing drug utilization, and processing claims, act as a principal in the arrangement on behalf of members in our other segments. As principal, our Healthcare Services segment reports revenues on a gross basis, including co-share amounts from members collected by third party retail pharmacies at the point of service.

In addition, our Healthcare Services intersegment revenues include revenues earned by certain owned providers derived from risk-based and non-risk-based managed care agreements with our health plans. Under risk-based agreements, the provider receives a monthly capitated fee that varies depending on the demographics and health status of the member, for each member assigned to these owned providers by our health plans. The owned provider assumes the economic risk of funding the assigned members’ healthcare services. Under non risk-based agreements, our health plans retain the economic risk of funding the assigned members' healthcare services. Our Healthcare Services segment reports provider services revenues associated with risk-based agreements on a gross basis, whereby capitation fee revenue is recognized in the period in which the assigned members are entitled to receive healthcare services. Provider services revenues associated with non-risk-based agreements are presented net of associated healthcare costs.

We present our condensed consolidated results of operations from the perspective of the health plans. As a result, the cost of providing benefits to our members, whether provided via a third party provider or internally through a stand-alone subsidiary, is classified as benefits expense and excludes the portion of the cost for which the health plans do not bear responsibility, including member co-share amounts and government subsidies of $4.0 billion and $3.5 billion for the three months ended September 30, 2019 and 2018, respectively. For the nine months ended September 30, 2019 and 2018 these amounts were $10.7 billion and $9.7 billion, respectively. In addition, depreciation and amortization expense associated with certain businesses in our Healthcare Services segment delivering benefits to our members, primarily associated with our provider services and pharmacy operations, are included with benefits expense. The amount of this expense was $32 million and $29 million for the three months ended September 30, 2019 and 2018, respectively. For the nine months ended September 30, 2019 and 2018, the amount of this expense was $92 million and $98 million, respectively.

Other than those described previously, the accounting policies of each segment are the same and are described in Note 2 to the consolidated financial statements included in our 2018 Form 10-K. Transactions between reportable segments primarily consist of sales of services rendered by our Healthcare Services segment, primarily pharmacy, provider, and clinical care services, to our Retail and Group and Specialty segment customers. Intersegment sales and expenses are recorded at fair value and eliminated in consolidation. Members served by our segments often use the same provider networks, enabling us in some instances to obtain more favorable contract terms with providers. Our segments also share indirect costs and assets. As a result, the profitability of each segment is interdependent. We allocate most operating expenses to our segments. Assets and certain corporate income and expenses are not allocated to the segments, including the portion of investment income not supporting segment operations, interest expense on corporate debt, and certain other corporate expenses. These items are managed at a corporate level. These corporate amounts are reported separately from our reportable segments and are included with intersegment eliminations in the tables presenting segment results below.

**Humana Inc.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**
**(Unaudited)**

Our segment results were as follows for the three and nine months ended September 30, 2019 and 2018:

| | Retail | Group and Specialty | Healthcare Services | Eliminations/ Corporate | Consolidated |
|---|---|---|---|---|---|
| | | | (in millions) | | |
| **Three months ended September 30, 2019** | | | | | |
| External revenues | | | | | |
| Premiums: | | | | | |
| Individual Medicare Advantage | $ 10,752 | $ — | $ — | $ — | $ 10,752 |
| Group Medicare Advantage | 1,609 | — | — | — | 1,609 |
| Medicare stand-alone PDP | 781 | — | — | — | 781 |
| Total Medicare | 13,142 | — | — | — | 13,142 |
| Fully-insured | 150 | 1,278 | — | — | 1,428 |
| Specialty | — | 400 | — | — | 400 |
| Medicaid and other | 742 | — | — | — | 742 |
| Total premiums | 14,034 | 1,678 | — | — | 15,712 |
| Services revenue: | | | | | |
| Provider | — | — | 136 | — | 136 |
| ASO and other | 4 | 200 | — | — | 204 |
| Pharmacy | — | — | 53 | — | 53 |
| Total services revenue | 4 | 200 | 189 | — | 393 |
| Total external revenues | 14,038 | 1,878 | 189 | — | 16,105 |
| Intersegment revenues | | | | | |
| Services | — | 4 | 4,654 | (4,658) | — |
| Products | — | — | 1,759 | (1,759) | — |
| Total intersegment revenues | — | 4 | 6,413 | (6,417) | — |
| Investment income | 50 | 7 | — | 79 | 136 |
| Total revenues | 14,088 | 1,889 | 6,602 | (6,338) | 16,241 |
| Operating expenses: | | | | | |
| Benefits | 12,050 | 1,448 | — | (141) | 13,357 |
| Operating costs | 1,310 | 413 | 6,348 | (6,182) | 1,889 |
| Depreciation and amortization | 89 | 24 | 43 | (29) | 127 |
| Total operating expenses | 13,449 | 1,885 | 6,391 | (6,352) | 15,373 |
| Income from operations | 639 | 4 | 211 | 14 | 868 |
| Interest expense | — | — | — | 62 | 62 |
| Other income, net | — | — | — | (82) | (82) |
| Income before income taxes and equity in net earnings | 639 | 4 | 211 | 34 | 888 |
| Equity in net earnings of Kindred at Home | — | — | 1 | — | 1 |
| Segment earnings | $ 639 | $ 4 | $ 212 | $ 34 | $ 889 |

**Humana Inc.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**
**(Unaudited)**

| | Retail | Group and Specialty | Healthcare Services | Individual Commercial | Other Businesses | Eliminations/ Corporate | Consolidated |
|---|---|---|---|---|---|---|---|
| | | | | (in millions) | | | |
| **Three months ended September 30, 2018** | | | | | | | |
| External revenues | | | | | | | |
| Premiums: | | | | | | | |
| Individual Medicare Advantage | $ 8,912 | $ — | $ — | $ — | $ — | $ — | $ 8,912 |
| Group Medicare Advantage | 1,542 | — | — | — | — | — | 1,542 |
| Medicare stand-alone PDP | 893 | — | — | — | — | — | 893 |
| Total Medicare | 11,347 | — | — | — | — | — | 11,347 |
| Fully-insured | 129 | 1,345 | — | 1 | — | — | 1,475 |
| Specialty | — | 325 | — | — | — | — | 325 |
| Medicaid and other | 561 | — | — | — | 4 | — | 565 |
| Total premiums | 12,037 | 1,670 | — | 1 | 4 | — | 13,712 |
| Services revenue: | | | | | | | |
| Provider | — | — | 113 | — | — | — | 113 |
| ASO and other | 1 | 215 | — | — | — | — | 216 |
| Pharmacy | — | — | 52 | — | — | — | 52 |
| Total services revenue | 1 | 215 | 165 | — | — | — | 381 |
| Total external revenues | 12,038 | 1,885 | 165 | 1 | 4 | — | 14,093 |
| Intersegment revenues | | | | | | | |
| Services | — | 4 | 4,214 | — | — | (4,218) | — |
| Products | — | — | 1,576 | — | — | (1,576) | — |
| Total intersegment revenues | — | 4 | 5,790 | — | — | (5,794) | — |
| Investment income | 35 | 5 | 11 | — | 10 | 52 | 113 |
| Total revenues | 12,073 | 1,894 | 5,966 | 1 | 14 | (5,742) | 14,206 |
| Operating expenses: | | | | | | | |
| Benefits | 10,020 | 1,347 | — | (4) | 12 | (132) | 11,243 |
| Operating costs | 1,352 | 445 | 5,720 | — | 2 | (5,619) | 1,900 |
| Depreciation and amortization | 67 | 21 | 40 | — | — | (26) | 102 |
| Total operating expenses | 11,439 | 1,813 | 5,760 | (4) | 14 | (5,777) | 13,245 |
| Income from operations | 634 | 81 | 206 | 5 | — | 35 | 961 |
| Gain on sale of business | — | — | — | — | — | (4) | (4) |
| Interest expense | — | — | — | — | — | 53 | 53 |
| Other expense, net | — | — | — | — | — | 11 | 11 |
| Income (loss) before income taxes and equity in net earnings | 634 | 81 | 206 | 5 | — | (25) | 901 |
| Equity in net earnings of Kindred at Home | — | — | 9 | — | — | — | 9 |
| Segment earnings (loss) | $ 634 | $ 81 | $ 215 | $ 5 | $ — | $ (25) | $ 910 |

**Humana Inc.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**
**(Unaudited)**

| | Retail | Group and Specialty | Healthcare Services | Eliminations/ Corporate | Consolidated |
|---|---|---|---|---|---|
| | | | (in millions) | | |
| **Nine months ended September 30, 2019** | | | | | |
| External revenues | | | | | |
| Premiums: | | | | | |
| Individual Medicare Advantage | $ 32,254 | $ — | $ — | $ — | $ 32,254 |
| Group Medicare Advantage | 4,867 | — | — | — | 4,867 |
| Medicare stand-alone PDP | 2,408 | — | — | — | 2,408 |
| Total Medicare | 39,529 | — | — | — | 39,529 |
| Fully-insured | 434 | 3,873 | — | — | 4,307 |
| Specialty | — | 1,160 | — | — | 1,160 |
| Medicaid and other | 2,143 | — | — | — | 2,143 |
| Total premiums | 42,106 | 5,033 | — | — | 47,139 |
| Services revenue: | | | | | |
| Provider | — | — | 367 | — | 367 |
| ASO and other | 14 | 587 | — | — | 601 |
| Pharmacy | — | — | 135 | — | 135 |
| Total services revenue | 14 | 587 | 502 | — | 1,103 |
| Total external revenues | 42,120 | 5,620 | 502 | — | 48,242 |
| Intersegment revenues | | | | | |
| Services | — | 13 | 13,456 | (13,469) | — |
| Products | — | — | 5,128 | (5,128) | — |
| Total intersegment revenues | — | 13 | 18,584 | (18,597) | — |
| Investment income | 139 | 17 | 1 | 194 | 351 |
| Total revenues | 42,259 | 5,650 | 19,087 | (18,403) | 48,593 |
| Operating expenses: | | | | | |
| Benefits | 36,396 | 4,177 | — | (405) | 40,168 |
| Operating costs | 3,664 | 1,232 | 18,371 | (18,015) | 5,252 |
| Depreciation and amortization | 239 | 67 | 121 | (84) | 343 |
| Total operating expenses | 40,299 | 5,476 | 18,492 | (18,504) | 45,763 |
| Income from operations | 1,960 | 174 | 595 | 101 | 2,830 |
| Interest expense | — | — | — | 184 | 184 |
| Other income, net | — | — | — | (217) | (217) |
| Income before income taxes and equity in net earnings | 1,960 | 174 | 595 | 134 | 2,863 |
| Equity in net earnings of Kindred at Home | — | — | 16 | — | 16 |
| Segment earnings | $ 1,960 | $ 174 | $ 611 | $ 134 | $ 2,879 |

**Humana Inc.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**
**(Unaudited)**

| | Retail | Group and Specialty | Healthcare Services | Individual Commercial | Other Businesses | Eliminations/ Corporate | Consolidated |
|---|---|---|---|---|---|---|---|
| | | | | (in millions) | | | |
| **Nine months ended September 30, 2018** | | | | | | | |
| External Revenues | | | | | | | |
| Premiums: | | | | | | | |
| Individual Medicare Advantage | $ 26,790 | $ — | $ — | $ — | $ — | $ — | $ 26,790 |
| Group Medicare Advantage | 4,575 | — | — | — | — | — | 4,575 |
| Medicare stand-alone PDP | 2,703 | — | — | — | — | — | 2,703 |
| Total Medicare | 34,068 | — | — | — | — | — | 34,068 |
| Fully-insured | 379 | 4,083 | — | 6 | — | — | 4,468 |
| Specialty | — | 1,014 | — | — | — | — | 1,014 |
| Medicaid and other | 1,664 | — | — | — | 22 | — | 1,686 |
| Total premiums | 36,111 | 5,097 | — | 6 | 22 | — | 41,236 |
| Services revenue: | | | | | | | |
| Provider | — | — | 290 | — | — | — | 290 |
| ASO and other | 6 | 642 | — | — | 4 | — | 652 |
| Pharmacy | — | — | 148 | — | — | — | 148 |
| Total services revenue | 6 | 642 | 438 | — | 4 | — | 1,090 |
| Total external revenues | 36,117 | 5,739 | 438 | 6 | 26 | — | 42,326 |
| Intersegment revenues | | | | | | | |
| Services | — | 13 | 12,426 | — | — | (12,439) | — |
| Products | — | — | 4,722 | — | — | (4,722) | — |
| Total intersegment revenues | — | 13 | 17,148 | — | — | (17,161) | — |
| Investment income | 102 | 18 | 34 | — | 110 | 154 | 418 |
| Total revenues | 36,219 | 5,770 | 17,620 | 6 | 136 | (17,007) | 42,744 |
| Operating expenses: | | | | | | | |
| Benefits | 30,842 | 3,977 | — | (73) | 77 | (374) | 34,449 |
| Operating costs | 3,784 | 1,355 | 16,910 | 3 | 6 | (16,648) | 5,410 |
| Depreciation and amortization | 199 | 66 | 125 | — | — | (88) | 302 |
| Total operating expenses | 34,825 | 5,398 | 17,035 | (70) | 83 | (17,110) | 40,161 |
| Income from operations | 1,394 | 372 | 585 | 76 | 53 | 103 | 2,583 |
| Loss on sale of business | — | — | — | — | — | 786 | 786 |
| Interest expense | — | — | — | — | — | 159 | 159 |
| Other expense, net | — | — | — | — | — | 11 | 11 |
| Income (loss) before income taxes and equity in net earnings | 1,394 | 372 | 585 | 76 | 53 | (853) | 1,627 |
| Equity in net earnings of Kindred at Home | — | — | 9 | — | — | — | 9 |
| Segment earnings (loss) | $ 1,394 | $ 372 | $ 594 | $ 76 | $ 53 | $ (853) | $ 1,636 |

**Humana Inc.**
**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The condensed consolidated financial statements of Humana Inc. in this document present the Company's financial position, results of operations and cash flows, and should be read in conjunction with the following discussion and analysis. References to "we," "us," "our," "Company," and "Humana" mean Humana Inc. and its subsidiaries. This discussion includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in filings with the Securities and Exchange Commission, or SEC, in our press releases, investor presentations, and in oral statements made by or with the approval of one of our executive officers, the words or phrases like "believes," "expects," "anticipates," "intends," "likely will result," "estimates," "projects" or variations of such words and similar expressions are intended to identify such forward–looking statements. These forward–looking statements are not guarantees of future performance and are subject to risks, uncertainties and assumptions, including, among other things, information set forth in Item 1A. – Risk Factors in our 2018 Form 10-K, as modified by any changes to those risk factors included in this document and in other reports we filed subsequent to February 21, 2019, in each case incorporated by reference herein. In making these statements, we are not undertaking to address or update such forward-looking statements in future filings or communications regarding our business or results. In light of these risks, uncertainties and assumptions, the forward–looking events discussed in this document might not occur. There may also be other risks that we are unable to predict at this time. Any of these risks and uncertainties may cause actual results to differ materially from the results discussed in the forward–looking statements.*

**Executive Overview**

***General***

Humana Inc., headquartered in Louisville, Kentucky, is a leading health and well-being company committed to helping our millions of medical and specialty members achieve their best health. Our successful history in care delivery and health plan administration is helping us create a new kind of integrated care with the power to improve health and well being and lower costs. Our efforts are leading to a better quality of life for people with Medicare, families, individuals, military service personnel, and communities at large. To accomplish that, we support physicians and other health care professionals as they work to deliver the right care in the right place for their patients, our members. Our range of clinical capabilities, resources and tools, such as in home care, behavioral health, pharmacy services, data analytics and wellness solutions, combine to produce a simplified experience that makes health care easier to navigate and more effective.

Our industry relies on two key statistics to measure performance. The benefit ratio, which is computed by taking total benefits expense as a percentage of premiums revenue, represents a statistic used to measure underwriting profitability. The operating cost ratio, which is computed by taking total operating costs, excluding depreciation and amortization, as a percentage of total revenue less investment income, represents a statistic used to measure administrative spending efficiency.

***Acquisitions and Divestitures***

In the third quarter of 2018, we completed the sale of our wholly-owned subsidiary KMG to CGIC. KMG's subsidiary, KIC, included our closed block of non-strategic commercial long-term care policies. Upon closing, we funded the transaction with approximately $190 million of parent company cash contributed into KMG, subject to customary adjustments, in addition to the transfer of approximately $160 million of statutory capital with the sale.

Also in the third quarter of 2018, we, along with TPG and WCAS, completed the acquisitions of Kindred and Curo, respectively, merging Curo with the hospice business of Kindred at Home. As part of these transactions, we acquired a 40% minority interest in Kindred at Home, a leading home health and hospice company, for total cash consideration of approximately $1.1 billion.

In the second quarter of 2018, we acquired FPG for cash consideration of approximately $185 million, net of cash received. FPG is one of the largest at-risk providers serving Medicare Advantage and Managed Medicaid HMO patients in Greater Orlando, Florida with a footprint that includes clinics located in Lake, Orange, Osceola and Seminole counties. The acquisition of FPG advances our strategy of helping physicians and clinicians evolve from treating health episodically to managing health holistically.

In the first quarter of 2018, we acquired the remaining equity interest in MCCI, a privately held management service organization headquartered in Miami, Florida, that primarily coordinates medical care for Medicare Advantage beneficiaries in Florida and Texas. The purchase price consisted primarily of $169 million cash, as well as our existing investment in MCCI and a note receivable and a revolving note with an aggregate balance of $383 million.

These transactions are more fully discussed in Note 1 and Note 3 to the condensed consolidated financial statements.

***Business Segments***

We manage our business with three reportable segments: Retail, Group and Specialty, and Healthcare Services. Beginning January 1, 2018, we exited the individual commercial fully-insured medical health insurance business, as well as certain other business, and therefore no longer report separately the Individual Commercial segment and the Other Business category in the current year. Previously, the Other Business category included businesses that were not individually reportable because they did not meet the quantitative thresholds required by generally accepted accounting principles, primarily our closed-block of commercial long-term care insurance policies which were sold in 2018. The reportable segments are based on a combination of the type of health plan customer and adjacent businesses centered on well-being solutions for our health plans and other customers, as described below. These segment groupings are consistent with information used by our Chief Executive Officer, the Chief Operating Decision Maker, to assess performance and allocate resources.

The Retail segment consists of Medicare benefits, marketed to individuals or directly via group Medicare accounts. In addition, the Retail segment also includes our contract with CMS to administer the Limited Income Newly Eligible Transition, or LI-NET, prescription drug plan program and contracts with various states to provide Medicaid, dual eligible, and Long-Term Support Services benefits, which we refer to collectively as our state-based contracts. The Group and Specialty segment consists of employer group commercial fully-insured medical and specialty health insurance benefits marketed to individuals and employer groups, including dental, vision, and other supplemental health benefits, as well as administrative services only, or ASO products. In addition, our Group and Specialty segment includes our military services business, primarily our TRICARE T2017 East Region contract. The Healthcare Services segment includes our services offered to our health plan members as well as to third parties, including pharmacy solutions, provider services, and clinical care service, such as home health and other services and capabilities to promote wellness and advance population health, including our minority investment in Kindred at Home. We reported under the category of Other Businesses those businesses that did not align with the reportable segments described above, primarily our closed-block long-term care insurance policies, which were sold in 2018.

The results of each segment are measured by segment earnings, and for our Healthcare Services Segment, also include the equity in net earnings of Kindred at Home. Transactions between reportable segments primarily consist of sales of services rendered by our Healthcare Services segment, primarily pharmacy, provider, and clinical care services, to our Retail and Group and Specialty segment customers. Intersegment sales and expenses are recorded at fair value and eliminated in consolidation. Members served by our segments often use the same provider networks, enabling us in some instances to obtain more favorable contract terms with providers. Our segments also share indirect costs and assets. As a result, the profitability of each segment is interdependent. We allocate most operating expenses to our segments. Assets and certain corporate income and expenses are not allocated to the segments, including the portion of investment income not supporting segment operations, interest expense on corporate debt, and certain other corporate expenses. These items are managed at a corporate level. These corporate amounts are reported separately from our reportable segments and are included with intersegment eliminations.

***Seasonality***

One of the product offerings of our Retail segment is Medicare stand-alone prescription drug plans, or PDPs, under the Medicare Part D program. Our quarterly Retail segment earnings and operating cash flows are impacted by the Medicare Part D benefit design and changes in the composition of our membership. The Medicare Part D benefit design results in coverage that varies as a member’s cumulative out-of-pocket costs pass through successive stages of a member’s plan period, which begins annually on January 1 for renewals. These plan designs generally result in us sharing a greater portion of the responsibility for total prescription drug costs in the early stages and less in the latter stages. As a result, the PDP benefit ratio generally decreases as the year progresses. In addition, the number of low-income senior members as well as year-over-year changes in the mix of membership in our stand-alone PDP products affects the quarterly benefit ratio pattern.

In addition, the Retail segment also experiences seasonality in the operating cost ratio as a result of costs incurred in the second half of the year associated with the Medicare marketing season.

Our Group and Specialty segment also experiences seasonality in the benefit ratio pattern. However, the effect is opposite of Medicare stand-alone PDP in the Retail segment, with the Group and Specialty segment's benefit ratio increasing as fully-insured members progress through their annual deductible and maximum out-of-pocket expenses.

***2019 Highlights***

- Our strategy offers our members affordable health care combined with a positive consumer experience in growing markets. At the core of this strategy is our integrated care delivery model, which unites quality care, high member engagement, and sophisticated data analytics. Our approach to primary, physician-directed care for our members aims to provide quality care that is consistent, integrated, cost-effective, and member-focused, provided by both employed physicians and physicians with network contract arrangements. The model is designed to improve health outcomes and affordability for individuals and for the health system as a whole, while offering our members a simple, seamless healthcare experience. We believe this strategy is positioning us for long-term growth in both membership and earnings. We offer providers a continuum of opportunities to increase the integration of care and offer assistance to providers in transitioning from a fee-for-service to a value-based arrangement. These include performance bonuses, shared savings and shared risk relationships. At September 30, 2019, approximately 2,340,600 members, or 66%, of our individual Medicare Advantage members were in value-based relationships under our integrated care delivery model, as compared to 2,010,800 members, or 66%, at September 30, 2018. Medicare Advantage and dual demonstration program membership enrolled in a Humana chronic care management program was 882,800 at September 30, 2019, an increase of 23.8% from 713,300 at September 30, 2018. These members may not be unique to each program since members have the ability to enroll in multiple programs. The increase is driven by our improved process for identifying and enrolling members in the appropriate program at the right time, coupled with growth in Special Needs Plans, or SNP, membership.

- In October 2019, the Centers for Medicare and Medicaid Services published its updated Medicare Star Ratings for bonus year 2021. We have 3.7 million members, or 92% of our Medicare Advantage membership as of August 2019, enrolled in 18 contracts that received a 4-star rating or above. In addition, we received a 5 out of 5-star rating for our CarePlus Health Plans, Inc. contract in Florida, and received a 4.5-star rating for six Medicare Advantage contracts offered in 19 states, which cover approximately 1.2 million members. The continued improvement in our Star ratings reflects our enterprise-wide focus on driving quality and improved health outcomes.

- Net income increased $867 million from $1.3 billion in 2018 to $2.2 billion in 2019 and earnings per diluted common share increased $6.66 from $9.58 earnings per diluted common share in 2018 to $16.24 earnings per diluted common share in 2019. This comparison was primarily impacted by our Medicare Advantage business and Healthcare Services segment, as well as by previously implemented productivity initiatives that led to significant operating cost efficiencies in 2019. These impacts were partially offset by strategic investments in our integrated care delivery model, the impact of higher compensation accruals for the Annual Incentive Plan, or AIP, offered to employees across all levels of the company, lower Group and Specialty segment earnings, and the impact of workforce optimization. These changes were further favorably impacted by the suspension of the health industry insurance fee in 2019 and by a lower number of shares used to compute dilutive earnings per share, primarily reflecting share repurchases. In addition, the 2019 period was impacted by the loss on the sale of KMG recognized in 2018.

- Contributing to our Retail segment revenue growth was our individual Medicare Advantage membership, which increased 508,700 members, or 16.7%, from September 30, 2018 to September 30, 2019.

- Our operating cash flow of $4.8 billion for 2019 improved primarily from the timing of working capital changes, higher earnings, and the impact of an approximately $245 million payment related to reinsuring certain voluntary benefit and financial protection products to a third party in connection with the sale of KMG in 2018.

- On July 31, 2019, we entered into an accelerated stock repurchase agreement, the July 2019 ASR, with Citibank, N.A., or Citi, to repurchase $1 billion of our common stock. On August 2, 2019, we made a payment of $1 billion to Citi and received an initial delivery of 2.7 million shares of our common stock. We expect final settlement under the agreement to occur during the fourth quarter of 2019.

- In August 2019, we issued $500 million of 3.125% senior notes due August 15, 2029 and $500 million of 3.950% senior notes due August 15, 2049. Our net proceeds, reduced for the underwriters discount and commission and offering expenses paid as of September 30, 2019, were $987 million.

- During the third quarter of 2019, we initiated an involuntary workforce optimization program that will allow us to promote operational excellence, accelerate our strategy, fund critical initiatives and advance our growth objectives. As a result we recorded estimated charges of $46 million, or $0.26 per diluted common share, on the corporate level, included with operating costs in the condensed consolidated statements of income. We expect this liability to be primarily paid within 12 months and classified it as a current liability, included in trade accounts payable and accrued expenses.

***Health Care Reform***

The Health Care Reform Law enacted significant reforms to various aspects of the U.S. health insurance industry. Certain significant provisions of the Health Care Reform Law include, among others, mandated coverage requirements, mandated benefits and guarantee issuance associated with commercial medical insurance, rebates to policyholders based on minimum benefit ratios, adjustments to Medicare Advantage premiums, the establishment of federally facilitated or state-based exchanges coupled with programs designed to spread risk among insurers, and the introduction of plan designs based on set actuarial values. In addition, the Health Care Reform Law established insurance industry assessments, including an annual health insurance industry fee. The annual health insurance industry fee levied on the insurance industry was $14.3 billion in 2018 and was not deductible for income tax purposes, which significantly increased our effective income tax rate. A one year suspension of the health insurance industry fee, as we experienced in 2017 and are experiencing in 2019, significantly impacts our trend in key operating metrics including our operating cost and medical expense ratios, as well as our effective tax rate. The annual health insurance industry fee is scheduled to resume for calendar year 2020 under current law.

It is reasonably possible that the Health Care Reform Law and related regulations, as well as future legislative, judicial or regulatory changes, including restrictions on our ability to manage our provider network or otherwise operate our business, or restrictions on profitability, including reviews by regulatory bodies that may compare our Medicare Advantage profitability to our non-Medicare Advantage business profitability, or compare the profitability of various products within our Medicare Advantage business, and require that they remain within certain ranges of each other, increases in member benefits or member eligibility criteria without corresponding increases in premium payments to us, or increases in regulation of our prescription drug benefit businesses, in the aggregate may have a material adverse effect on our results of operations (including restricting revenue, enrollment and premium growth in certain products and market segments, restricting our ability to expand into new markets, increasing our medical and operating costs, further lowering our Medicare payment rates and increasing our expenses associated with the non-deductible health insurance industry fee and other assessments); our financial position (including our ability to maintain the value of our goodwill); and our cash flows.

We intend for the discussion of our financial condition and results of operations that follows to assist in the understanding of our financial statements and related changes in certain key items in those financial statements from year to year, including the primary factors that accounted for those changes. Transactions between reportable segments primarily consist of sales of services rendered by our Healthcare Services segment, primarily pharmacy, provider, and clinical care services, to our Retail and Group and Specialty segment customers and are described in Note 15 to the condensed consolidated financial statements included in this report.

**Comparison of Results of Operations for 2019 and 2018**

The following discussion primarily deals with our results of operations for the three months ended September 30, 2019, or the 2019 quarter, the three months ended September 30, 2018, or the 2018 quarter, the nine months ended September 30, 2019, or the 2019 period, and the nine months ended September 30, 2018, or the 2018 period.

***Consolidated***

| | For the three months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (dollars in millions, except per common share results) | | | |
| Revenues: | | | | |
| Premiums: | | | | |
| Retail | $ 14,034 | $ 12,037 | $ 1,997 | 16.6 % |
| Group and Specialty | 1,678 | 1,670 | 8 | 0.5 % |
| Individual Commercial | — | 1 | (1) | (100.0)% |
| Other Businesses | — | 4 | (4) | (100.0)% |
| Total premiums | 15,712 | 13,712 | 2,000 | 14.6 % |
| Services: | | | | |
| Retail | 4 | 1 | 3 | 300.0 % |
| Group and Specialty | 200 | 215 | (15) | (7.0)% |
| Healthcare Services | 189 | 165 | 24 | 14.5 % |
| Total services | 393 | 381 | 12 | 3.1 % |
| Investment income | 136 | 113 | 23 | 20.4 % |
| Total revenues | 16,241 | 14,206 | 2,035 | 14.3 % |
| Operating expenses: | | | | |
| Benefits | 13,357 | 11,243 | 2,114 | 18.8 % |
| Operating costs | 1,889 | 1,900 | (11) | (0.6)% |
| Depreciation and amortization | 127 | 102 | 25 | 24.5 % |
| Total operating expenses | 15,373 | 13,245 | 2,128 | 16.1 % |
| Income from operations | 868 | 961 | (93) | (9.7)% |
| Gain on sale of business | — | (4) | 4 | (100.0)% |
| Interest expense | 62 | 53 | 9 | 17.0 % |
| Other (income) expense, net | (82) | 11 | (93) | (845.5)% |
| Income before income taxes and equity in net earnings | 888 | 901 | (13) | (1.4)% |
| Provision for income taxes | 200 | 266 | (66) | (24.8)% |
| Equity in net earnings of Kindred at Home | 1 | 9 | (8) | (88.9)% |
| Net income | $ 689 | $ 644 | $ 45 | 7.0 % |
| Diluted earnings per common share | $ 5.14 | $ 4.65 | $ 0.49 | 10.5 % |
| Benefit ratio (a) | 85.0% | 82.0% | | 3.0 % |
| Operating cost ratio (b) | 11.7% | 13.5% | | (1.8)% |
| Effective tax rate | 22.5% | 29.1% | | (6.6)% |

(a) Represents benefits expense as a percentage of premiums revenue.
(b) Represents operating costs as a percentage of total revenues less investment income.

| | For the nine months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (dollars in millions, except per common share results) | | | |
| Revenues: | | | | |
| Premiums: | | | | |
| Retail | $ 42,106 | $ 36,111 | $ 5,995 | 16.6 % |
| Group and Specialty | 5,033 | 5,097 | (64) | (1.3)% |
| Individual Commercial | — | 6 | (6) | (100.0)% |
| Other Businesses | — | 22 | (22) | (100.0)% |
| Total premiums | 47,139 | 41,236 | 5,903 | 14.3 % |
| Services: | | | | |
| Retail | 14 | 6 | 8 | 133.3 % |
| Group and Specialty | 587 | 642 | (55) | (8.6)% |
| Healthcare Services | 502 | 438 | 64 | 14.6 % |
| Other Businesses | — | 4 | (4) | (100.0)% |
| Total services | 1,103 | 1,090 | 13 | 1.2 % |
| Investment income | 351 | 418 | (67) | (16.0)% |
| Total revenues | 48,593 | 42,744 | 5,849 | 13.7 % |
| Operating expenses: | | | | |
| Benefits | 40,168 | 34,449 | 5,719 | 16.6 % |
| Operating costs | 5,252 | 5,410 | (158) | (2.9)% |
| Depreciation and amortization | 343 | 302 | 41 | 13.6 % |
| Total operating expenses | 45,763 | 40,161 | 5,602 | 13.9 % |
| Income from operations | 2,830 | 2,583 | 247 | 9.6 % |
| Loss on sale of business | — | 786 | (786) | (100.0)% |
| Interest expense | 184 | 159 | 25 | 15.7 % |
| Other (income) expense, net | (217) | 11 | (228) | (2,072.7)% |
| Income before income taxes and equity in net earnings | 2,863 | 1,627 | 1,236 | 76.0 % |
| Provision for income taxes | 684 | 308 | 376 | 122.1 % |
| Equity in net earnings of Kindred at Home | 16 | 9 | 7 | 77.8 % |
| Net income | $ 2,195 | $ 1,328 | $ 867 | 65.3 % |
| Diluted earnings per common share | $ 16.24 | $ 9.58 | $ 6.66 | 69.5 % |
| Benefit ratio (a) | 85.2% | 83.5% | | 1.7 % |
| Operating cost ratio (b) | 10.9% | 12.8% | | (1.9)% |
| Effective tax rate | 23.8% | 18.8% | | 5.0 % |

(a) Represents benefits expense as a percentage of premiums revenue.
(b) Represents operating costs as a percentage of total revenues less investment income.

*Summary*

Net income was $689 million, or $5.14 per diluted common share, in the 2019 quarter compared to $644 million, or $4.65 per diluted common share, in the 2018 quarter. Net income was $2.2 billion, or $16.24 per diluted common share, in the 2019 period compared to $1.3 billion, or $9.58 per diluted common share, in the 2018 period. These increases were primarily impacted by our Medicare Advantage business and Healthcare Services segment, as well as by previously implemented productivity initiatives that led to significant operating cost efficiencies in 2019. These impacts were partially offset by strategic investments in our integrated care delivery model, the impact of higher compensation accruals for the AIP offered to employees across all levels of the company, lower Group and Specialty segment earnings, and the impact of workforce optimization. These changes were further favorably impacted by the suspension of the health industry insurance fee in 2019 and by a lower number of shares used to compute dilutive earnings per share, primarily reflecting share repurchases. In addition, the 2019 period was impacted by the loss on the sale of KMG recognized in 2018.

*Premiums Revenue*

Consolidated premiums increased $2.0 billion, or 14.6%, from the 2018 quarter to $15.7 billion for the 2019 quarter and increased $5.9 billion, or 14.3%, from the 2018 period to $47.1 billion for the 2019 period primarily due to higher premiums in the Retail segment, driven by higher premium revenues from out Medicare Advantage business resulting from membership growth and higher per member premiums. These increases were partially offset by the impact of declining stand-alone PDP membership year-over-year, as well as lower premiums in the Group and Specialty segment in the 2019 period as discussed in the detailed segment results discussion that follows.

*Services Revenue*

Consolidated services revenue increased $12 million, or 3.1%, from the 2018 quarter to $393 million for the 2019 quarter primarily due to an increase in services revenue in the Healthcare Services segment, partially offset by a decline in the Group and Specialty segment as detailed in the segment results discussion that follows. Consolidated services revenue was relatively unchanged at $1.10 billion for the 2019 period increasing $13 million, or 1.2%, from the 2018 period due to increased services revenue in the Healthcare Services segment, partially offset by a decline in the Group and Specialty segment as detailed in the segment results discussion that follows.

*Investment Income*

Investment income totaled $136 million for the 2019 quarter, increasing $23 million, or 20.4%, from $113 million for the 2018 quarter. This increase primarily reflects higher realized capital gains, higher average invested capital balances, and higher interest rates. For the 2019 period, investment income totaled $351 million, decreasing $67 million, or 16.0%, from $418 million in the 2018 period. This decrease primarily reflects lower realized capital gains and lower average invested balances, partially offset by higher interest rates.

*Benefits Expense*

Consolidated benefits expense was $13.4 billion for the 2019 quarter, an increase of $2.1 billion from the 2018 quarter. For the 2019 period, benefits expense was $40.2 billion, an increase of $5.7 billion from the 2018 period. The consolidated benefit ratio for the 2019 quarter of 85.0% increased 300 basis points from 82.0% in the 2018 quarter. The consolidated benefit ratio for the 2019 period increased 170 basis points to 85.2% from 83.5% in the 2018 period. These increases were primarily due to the suspension of the health insurance industry fee in 2019, which was contemplated in the pricing and benefit design of our products, lower favorable prior-period medical claims reserve development, an increase in the Group and Specialty benefit ratio as discussed in the detailed segment results discussion that follows, and the shift in Medicare membership mix, due to the loss of stand-alone PDP members and significant growth in Medicare Advantage members. These increases were partially offset by engaging our Medicare Advantage members in clinical programs, as well as ensuring they are appropriately documented under the CMS risk-adjustment model, and lower than expected medical costs as compared to the assumptions used in the pricing of our individual Medicare Advantage business for 2019. In addition, the 2019 quarter was significantly negatively impacted by weekday seasonality.

The favorable prior-period medical claims reserve development decreased the consolidated benefit ratio by approximately 40 basis points in the 2019 quarter versus approximately 90 basis points in the 2018 quarter. The favorable prior-period medical claims reserve development decreased the consolidated benefit ratio by approximately 70 basis points to 85.2% for the 2019 period compared to approximately 110 basis points to 83.5% for the 2018 period.

*Operating Costs*

Our segments incur both direct and shared indirect operating costs. We allocate the indirect costs shared by the segments primarily as a function of revenues. As a result, the profitability of each segment is interdependent.

Consolidated operating costs decreased $11 million, or 0.6%, during the 2019 quarter compared to the 2018 quarter and decreased $158 million, or 2.9%, during the 2019 period compared to the 2018 period. These decreases were primarily due to a decrease in operating costs in the Retail and the Group and Specialty segments as discussed in the detailed segment results discussion that follows.

The consolidated operating cost ratio for the 2019 quarter of 11.7% decreased 180 basis points from 13.5% in the 2018 quarter and for the 2019 period decreased 190 basis points to 10.9% from 12.8% in the 2018 period. These decreases were primarily due to the suspension of the health insurance industry fee in 2019, scale efficiencies associated with growth in our Medicare Advantage membership, and significant operating cost efficiencies in 2019 driven by previously implemented productivity initiatives. These improvements were partially offset by strategic investments in our integrated care delivery model, the impact of higher compensation expense accruals in the 2019 quarter for the AIP offered to employees across all levels, and charges associated with workforce optimization. The higher compensation accruals resulted from our continued strong performance, including customer satisfaction as measured by the net promoter score, along with higher than anticipated individual Medicare Advantage membership growth. The non-deductible health insurance industry fee impacted the operating cost ratio by 180 basis points in both the 2018 quarter and period.

*Depreciation and Amortization*

Depreciation and amortization for the 2019 quarter totaled $127 million compared to $102 million for the 2018 quarter. For the 2019 period, depreciation and amortization totaled $343 million compared to $302 million for the 2018 period. We accelerated the depreciation related to certain capitalized software of $19 million in the 2019 quarter and period.

*Interest Expense*

Interest expense for the 2019 quarter of $62 million increased $9 million, compared to $53 million for the 2018 quarter. Interest expense for the 2019 period of $184 million increased $25 million, compared to $159 million for the 2018 period. These increases were primarily due to the higher average borrowings outstanding including the impact of the borrowings under the November 2018 term loan agreement and senior notes issued in August 2019.

*Income Taxes*

The effective income tax rate was 22.5% and 23.8% for the three and nine months ended September 30, 2019, respectively, compared to 29.1% and 18.8% for the three and nine months ended September 30, 2018, respectively. These changes primarily reflect the impact of the suspension of the non-deductible health insurance industry fee in 2019 as well as the deferred tax benefit recognized in 2018 from the loss on sale of KMG. The effective income tax rate for the nine months ended September 30, 2018 reflected a $430 million deferred tax benefit, resulting from the loss on the sale of KMG attributable to its original tax basis and subsequent capital contributions to fund accumulated losses.

***Retail Segment***

| | September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Members | Percentage |
| **Membership:** | | | | |
| Medical membership: | | | | |
| Individual Medicare Advantage | 3,552,500 | 3,043,800 | 508,700 | 16.7 % |
| Group Medicare Advantage | 523,900 | 496,800 | 27,100 | 5.5 % |
| Medicare stand-alone PDP | 4,379,800 | 5,015,900 | (636,100) | (12.7)% |
| Total Retail Medicare | 8,456,200 | 8,556,500 | (100,300) | (1.2)% |
| State-based Medicaid | 469,000 | 323,800 | 145,200 | 44.8 % |
| Medicare Supplement | 286,600 | 246,600 | 40,000 | 16.2 % |
| Total Retail medical members | 9,211,800 | 9,126,900 | 84,900 | 0.9 % |

| | For the three months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (in millions) | | | |
| **Premiums and Services Revenue:** | | | | |
| Premiums: | | | | |
| Individual Medicare Advantage | $ 10,752 | $ 8,912 | $ 1,840 | 20.6 % |
| Group Medicare Advantage | 1,609 | 1,542 | 67 | 4.3 % |
| Medicare stand-alone PDP | 781 | 893 | (112) | (12.5)% |
| Total Retail Medicare | 13,142 | 11,347 | 1,795 | 15.8 % |
| State-based Medicaid | 742 | 561 | 181 | 32.3 % |
| Medicare Supplement | 150 | 129 | 21 | 16.3 % |
| Total premiums | 14,034 | 12,037 | 1,997 | 16.6 % |
| Services | 4 | 1 | 3 | 300.0 % |
| Total premiums and services revenue | $ 14,038 | $ 12,038 | $ 2,000 | 16.6 % |
| **Segment earnings** | $ 639 | $ 634 | $ 5 | 0.8 % |
| Benefit ratio | 85.9% | 83.2% | | 2.7 % |
| Operating cost ratio | 9.3% | 11.2% | | (1.9)% |

| | For the nine months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (in millions) | | | |
| **Premiums and Services Revenue:** | | | | |
| Premiums: | | | | |
| Individual Medicare Advantage | $ 32,254 | $ 26,790 | $ 5,464 | 20.4 % |
| Group Medicare Advantage | 4,867 | 4,575 | 292 | 6.4 % |
| Medicare stand-alone PDP | 2,408 | 2,703 | (295) | (10.9)% |
| Total Retail Medicare | 39,529 | 34,068 | 5,461 | 16.0 % |
| State-based Medicaid | 2,143 | 1,664 | 479 | 28.8 % |
| Medicare Supplement | 434 | 379 | 55 | 14.5 % |
| Total premiums | 42,106 | 36,111 | 5,995 | 16.6 % |
| Services | 14 | 6 | 8 | 133.3 % |
| Total premiums and services revenue | $ 42,120 | $ 36,117 | $ 6,003 | 16.6 % |
| **Segment earnings** | $ 1,960 | $ 1,394 | $ 566 | 40.6 % |
| Benefit ratio | 86.4% | 85.4% | | 1.0 % |
| Operating cost ratio | 8.7% | 10.5% | | (1.8)% |

*Segment Earnings*

- Retail segment earnings increased $5 million, or 0.8%, from $634 million in the 2018 quarter to $639 million in the 2019 quarter. Retail segment earnings increased $566 million, or 40.6%, from $1.4 billion in the 2018 period to $2.0 billion in the 2019 period. These increases primarily reflect the lower operating cost ratio, partially offset by the higher benefit ratio as more fully described below. As expected, the higher-than-anticipated individual Medicare Advantage membership growth during the previous Annual Election Period, or AEP, had a muted impact on the segment's earnings in the 2019 period. While new Medicare Advantage members increase revenue, on average, they have a break even impact on segment earnings in the first year as they were not previously engaged in a clinical programs or appropriately documented under the CMS risk-adjustment model, and accordingly, carry a higher benefit ratio.

*Enrollment*

- Individual Medicare Advantage membership increased 508,700 members, or 16.7%, from September 30, 2018 to September 30, 2019, primarily due to membership additions associated with the previous AEP and Open Election Period, or OEP, for Medicare beneficiaries. The OEP sales period, which ran from January 1 to March 31, added approximately 43,700 members. Since March 31, 2019, enrollment has continued to increase due to strong sales to age-ins and those eligible for Dual Eligible Special Need Plans, or D-SNP. Individual Medicare Advantage membership includes 280,700 D-SNP members as of September 30, 2019, a net increase of 69,300, or 32.8%, from 211,400 as of September 30, 2018.

- Group Medicare Advantage membership increased 27,100, or 5.5%, from September 30, 2018 to September 30, 2019, primarily due to net membership additions associated with the previous AEP for Medicare beneficiaries.

- Medicare stand-alone PDP membership decreased 636,100 members, or 12.7%, from September 30, 2018 to September 30, 2019 reflecting net declines during the previous AEP for Medicare beneficiaries. These anticipated declines were primarily due to the competitive nature of the industry and the pricing discipline we have employed, which resulted in us no longer being the low cost plan in any market for 2019.

- State-based Medicaid membership increased 145,200 members, or 44.8%, from September 30, 2018 to September 30, 2019, primarily driven by the statewide award of a comprehensive contract under the Managed Medical Assistance, or MMA, program in Florida.

*Premiums Revenue*

- Retail segment premiums increased $2.0 billion, or 16.6%, from the 2018 quarter to the 2019 quarter and increased $6.0 billion, or 16.6%, from the 2018 period to the 2019 period primarily due to Medicare Advantage membership growth and higher per member premiums, as well as increased state-based contracts membership. These favorable items were partially offset by the decline in membership in our stand-alone PDP offerings.

*Benefits Expense*

- The Retail segment benefit ratio increased 270 basis points from 83.2% in the 2018 quarter to 85.9% in the 2019 quarter primarily due to the suspension of the health insurance industry fee in 2019 which was contemplated in the pricing and benefit design of our products, the significant unfavorable impact in the 2019 quarter of weekday seasonality, lower favorable prior-period medical claims reserve development, as well as the shift in Medicare membership mix due to the loss of stand-alone PDP members and the significant growth in Medicare Advantage members. These increases were partially offset by engaging our Medicare Advantage members in clinical programs as well as ensuring they are appropriately documented under the CMS risk-adjustment model, and lower than expected medical costs as compared to the assumptions used in the pricing of our individual Medicare Advantage business for 2019. The Retail segment benefit ratio increased 100 basis points from 85.4% in the 2018 period to 86.4% in the 2019 period, primarily reflecting the same factors that affected the 2019 quarter described above, but excluding the impact of weekday seasonality. These factors were partially offset by the impact of a less severe flu season in the 2019 period.

- The Retail segment's benefits expense for the 2019 quarter included $55 million in favorable prior-period medical claims reserve development versus $120 million in the 2018 quarter. For the 2019 period, the benefits expense includes the beneficial effect of $366 million in favorable prior-period medical claims reserve development versus $367 million in the 2018 period. Prior-period medical claims reserve development decreased the Retail segment benefit ratio by approximately 40 basis points in the 2019 quarter versus approximately 100 basis points in the 2018 quarter. Favorable prior-period medical claims reserve development decreased the Retail segment benefit ratio by approximately 90 basis points in the 2019 period versus approximately 100 basis points in the 2018 period.

*Operating Costs*

- The Retail segment operating cost ratio of 9.3% for the 2019 quarter decreased 190 basis points from 11.2% for the 2018 quarter. The Retail segment operating cost ratio of 8.7% for the 2019 period decreased 180 basis points from 10.5% for the 2018 period. These decreases primarily were due to the suspension of the health insurance industry fee in 2019, as well as scale efficiencies associated with growth in our Medicare Advantage membership, and significant operating costs efficiencies in 2019 driven by previously implemented productivity initiatives. These decreases were partially offset by the strategic investments in our integrated care delivery model and the impact of higher compensation expense accruals in 2019 for the AIP as a result of our continued strong performance. The non-deductible health insurance industry fee impacted the operating cost ratio by 190 basis points in the 2018 quarter and period.

***Group and Specialty Segment***

| | September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Members | Percentage |
| **Membership:** | | | | |
| Medical membership: | | | | |
| Fully-insured commercial group | 927,400 | 1,029,100 | (101,700) | (9.9)% |
| ASO | 516,800 | 449,900 | 66,900 | 14.9 % |
| Military services | 5,998,700 | 5,927,400 | 71,300 | 1.2 % |
| Total group and specialty medical members | 7,442,900 | 7,406,400 | 36,500 | 0.5 % |
| Specialty membership (a) | 5,411,400 | 6,116,300 | (704,900) | (11.5)% |

(a) Specialty products include dental, vision, voluntary benefit products and other supplemental health. Members included in these products may not be unique to each product since members have the ability to enroll in multiple products.

| | For the three months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (in millions) | | | |
| **Premiums and Services Revenue:** | | | | |
| Premiums: | | | | |
| Fully-insured commercial group | $ 1,278 | $ 1,345 | $ (67) | (5.0)% |
| Group specialty | 400 | 325 | 75 | 23.1 % |
| Total premiums | 1,678 | 1,670 | 8 | 0.5 % |
| Services | 200 | 215 | (15) | (7.0)% |
| Total premiums and services revenue | $ 1,878 | $ 1,885 | $ (7) | (0.4)% |
| **Segment earnings** | $ 4 | $ 81 | $ (77) | (95.1)% |
| Benefit ratio | 86.3% | 80.7% | | 5.6 % |
| Operating cost ratio | 21.9% | 23.6% | | (1.7)% |

| | For the nine months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (in millions) | | | |
| **Premiums and Services Revenue:** | | | | |
| Premiums: | | | | |
| Fully-insured commercial group | $ 3,873 | $ 4,083 | $ (210) | (5.1)% |
| Group specialty | 1,160 | 1,014 | 146 | 14.4 % |
| Total premiums | 5,033 | 5,097 | (64) | (1.3)% |
| Services | 587 | 642 | (55) | (8.6)% |
| Total premiums and services revenue | $ 5,620 | $ 5,739 | $ (119) | (2.1)% |
| **Segment earnings** | $ 174 | $ 372 | $ (198) | (53.2)% |
| Benefit ratio | 83.0% | 78.0% | | 5.0 % |
| Operating cost ratio | 21.9% | 23.6% | | (1.7)% |

*Segment Earnings*

- Group and Specialty segment earnings decreased $77 million, or 95.1%, from $81 million in the 2018 quarter to $4 million in the 2019 quarter. Group and Specialty segment earnings decreased $198 million, or 53.2%, from $372 million in the 2018 period to $174 million in the 2019 period. These decreases were primarily due to a higher benefit ratio, along with lower military services business earnings. Earnings comparisons related to the military services business were unfavorably impacted by the receipt of certain contractual incentives and adjustments in 2018 related to the previous TRICARE contract which did not recur in 2019. These decreases were partially offset by the improvement in the operating cost ratio as more fully described below.

*Enrollment*

- Fully-insured commercial group medical membership decreased 101,700 members, or 9.9%, from September 30, 2018 to September 30, 2019 primarily reflecting lower membership in small group accounts due in part to more small group accounts selecting level-funded ASO products in 2019, as well as the loss of certain large group accounts due to the competitive pricing environment. The portion of group fully-insured commercial medical membership in small group accounts was approximately 60% at September 30, 2019 and 62% at September 30, 2018.

- Group ASO commercial medical membership increased 66,900 members, or 14.9%, from September 30, 2018 to September 30, 2019 reflecting more small group accounts selecting level-funded ASO products in 2019, partially offset by the loss of certain large group accounts as a result of continued discipline in pricing of services for self-funded accounts amid a highly competitive environment.

- Military services membership increased 71,300 members, or 1.2%, from September 30, 2018 to September 30, 2019. Membership includes military service members, retirees, and their families to whom the company provides healthcare services under the current T2017 TRICARE East Region contract. The current contract, which covers 32 states, became effective on January 1, 2018.

- Specialty membership decreased 704,900 members, or 11.5%, from September 30, 2018 to September 30, 2019 primarily due to the loss of certain group accounts, including one jumbo account, offering stand-alone dental and vision products.

*Premiums Revenue*

- Group and Specialty segment premiums were relatively unchanged increasing $8 million, or 0.5%, from the 2018 quarter to $1.7 billion for the 2019 quarter. Group and Specialty segment premiums decreased $64 million, or 1.3%, from the 2018 period to $5.0 billion for the 2019 period, primarily due to a decline in our fully-insured group commercial and specialty membership. This decrease was partially offset by higher stop-loss revenues related to our level-funded ASO accounts resulting from membership growth in this product, higher per member premiums across the fully-insured business, and lower unfavorable commercial risk adjustment, or CRA, payable estimate in 2019 as compared to 2018, which resulted in higher small group fully-insured commercial revenues. The 2019 period was further negatively impacted by the exit of our voluntary benefit and financial protection products in connection with the sale of KMG in 2018.

*Services Revenue*

- Group and Specialty segment services revenue decreased $15 million, or 7.0%, from the 2018 quarter to $200 million for the 2019 quarter and decreased $55 million, or 8.6%, from the 2018 period to $587 million for the 2019 period primarily due to the impact of certain contractual incentives and adjustments related to the previous TRICARE contract received in 2018, which did not recur in 2019.

*Benefits Expense*

- The Group and Specialty segment benefit ratio increased 560 basis points from 80.7% in the 2018 quarter to 86.3% in the 2019 quarter. The Group and Specialty segment benefit ratio increased 500 basis points from 78.0% in the 2018 period to 83.0% in the 2019 period. These increases primarily were due to the significant unfavorable impact in the 2019 quarter of weekday seasonality, the suspension of the health insurance industry fee in 2019 which was contemplated in the pricing and benefit design of our products, as well as the meaningful impact of the continued migration of fully-insured group members to level-funded ASO products in 2019 resulting in a membership mix transformation. In addition, the impact of adjustments to dental network contracted rates resulting from dental network re-contracting and expansion to position the business for the future, and lower prior-period medical claims reserve development unfavorably impacted the 2019 quarter and period ratio. These items were partially offset by the smaller unfavorable premium adjustment in 2019 as compared to 2018 related to our CRA accrual associated with the ACA-compliant business as a result of the release of CMS's final 2018 CRA data.
- The Group and Specialty segment's benefits expense included $1 million in favorable prior-period medical claims reserve development in the 2019 quarter versus $7 million in the 2018 quarter. This favorable prior-period medical claims reserve development decreased the Group and Specialty segment benefit ratio by approximately 10 basis points in the 2019 quarter and approximately 40 basis points in the 2018 quarter. The Group and Specialty segment's benefits expense included the effect of an unfavorable prior-period medical claims reserve development of $35 million in the 2019 period versus favorable prior-period medical claims reserve development of $41 million in the 2018 period. The unfavorable prior-period medical claims reserve development for the 2019 period increased the Group and Specialty segment benefit ratio by approximately 70 basis points and the favorable prior-period medical claims reserve development for the 2018 period decreased the Group and Specialty segment benefit ratio 80 basis points.

*Operating Costs*

- The Group and Specialty segment operating cost ratio of 21.9% for the 2019 quarter decreased 170 basis points from 23.6% for the 2018 quarter. For the 2019 period, the Group and Specialty segment operating cost ratio of 21.9% decreased 170 basis points from 23.6% for the 2018 period. These decreases primarily were due to the suspension of the health insurance industry fee in 2019, as well as significant operating cost efficiencies in the 2019 quarter driven by previously implemented productivity initiatives. These improvements were offset by the higher compensation expense accruals in 2019 for the AIP as a result of our continued strong performance. The 2019 period was further impacted by the exit of our voluntary benefit and financial protection products in connection with the sale of KMG in 2018, which carried a higher operating cost ratio. The non-deductible health insurance industry fee impacted the operating cost ratio by 160 basis points in the 2018 quarter and period.

***Healthcare Services Segment***

| | For the three months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (in millions) | | | |
| **Revenues:** | | | | |
| Services: | | | | |
| Provider services | $ 104 | $ 70 | $ 34 | 48.6 % |
| Pharmacy solutions | 53 | 52 | 1 | 1.9 % |
| Clinical care services | 32 | 43 | (11) | (25.6)% |
| Total services revenues | 189 | 165 | 24 | 14.5 % |
| Intersegment revenues: | | | | |
| Pharmacy solutions | 5,673 | 5,092 | 581 | 11.4 % |
| Provider services | 591 | 537 | 54 | 10.1 % |
| Clinical care services | 149 | 161 | (12) | (7.5)% |
| Total intersegment revenues | 6,413 | 5,790 | 623 | 10.8 % |
| Total services and intersegment revenues | $ 6,602 | $ 5,955 | $ 647 | 10.9 % |
| **Segment earnings** | $ 212 | $ 215 | $ (3) | (1.4)% |
| Operating cost ratio | 96.2% | 96.1% | | 0.1 % |

| | For the nine months ended September 30, | | Change | |
|---|---|---|---|---|
| | 2019 | 2018 | Dollars | Percentage |
| | (in millions) | | | |
| **Revenues:** | | | | |
| Services: | | | | |
| Provider services | $ 265 | $ 158 | $ 107 | 67.7 % |
| Pharmacy solutions | 134 | 148 | (14) | (9.5)% |
| Clinical care services | 103 | 132 | (29) | (22.0)% |
| Total services revenues | 502 | 438 | 64 | 14.6 % |
| Intersegment revenues: | | | | |
| Pharmacy solutions | 16,335 | 15,181 | 1,154 | 7.6 % |
| Provider services | 1,792 | 1,456 | 336 | 23.1 % |
| Clinical care services | 457 | 511 | (54) | (10.6)% |
| Total intersegment revenues | 18,584 | 17,148 | 1,436 | 8.4 % |
| Total services and intersegment revenues | $ 19,086 | $ 17,586 | $ 1,500 | 8.5 % |
| **Segment earnings** | $ 611 | $ 594 | $ 17 | 2.9 % |
| Operating cost ratio | 96.3% | 96.2% | | 0.1 % |

*Segment Earnings*

- Healthcare Services segment earnings of $212 million for the 2019 quarter was relatively unchanged, decreasing $3 million, or 1.4%, from $215 million in the 2018 quarter. The decrease primarily resulted from additional investments in clinical assets associated with our provider services business and slightly lower earnings from Kindred at Home operations. These declines were partially offset by higher earnings from our pharmacy operations and the improvement in core operating results from the provider services business year over year. For the 2019 period, the Healthcare Services segment earnings of $611 million increased $17 million, or 2.9%, from $594 million in the 2018 period. This increase was primarily due to higher earnings from our pharmacy and clinical care services operations and 2019 earnings from Kindred at Home operations. These factors were partially offset by additional investments in new clinical assets associated with our provider services business.

*Script Volume*

- Humana Pharmacy Solutions script volumes on an adjusted 30-day equivalent basis increased to approximately 116 million in the 2019 quarter, up 5.5%, versus scripts of approximately 110 million in the 2018 quarter. For the 2019 period, script volumes increased to approximately 339 million, up 3.4%, versus scripts of approximately 328 million in the 2018 period. These increases primarily reflect growth associated with higher individual Medicare Advantage membership, partially offset by the decline in stand-alone PDP membership.

*Services Revenues*

- Services revenues increased $24 million, or 14.5%, from the 2018 quarter to $189 million for the 2019 quarter and increased $64 million, or 14.6%, from the 2018 period to $502 million for the 2019 period primarily due to revenue growth from our provider services business.

*Intersegment Revenues*

- Intersegment revenues increased $623 million, or 10.8%, from the 2018 quarter to $6.4 billion for the 2019 quarter and increased $1.4 billion, or 8.4%, from the 2018 period to $18.6 billion for the 2019 period. These increases primarily were due to strong Medicare Advantage membership growth, partially offset by the loss of intersegment revenues associated with the decline in stand-alone PDP membership. The 2019 period was further impacted by higher revenues associated with our provider services business reflecting the previously disclosed acquisition of MCCI and FPG.

*Operating Costs*

- The Healthcare Services segment operating cost ratio of 96.2% and 96.3% for the 2019 quarter and period, respectively, were relatively unchanged from 96.1% and 96.2% in the 2018 quarter and period, respectively.

**Liquidity**

Historically, our primary sources of cash have included receipts of premiums, services revenue, and investment and other income, as well as proceeds from the sale or maturity of our investment securities, and borrowings. Our primary uses of cash historically have included disbursements for claims payments, operating costs, interest on borrowings, taxes, purchases of investment securities, acquisitions, capital expenditures, repayments on borrowings, dividends, and share repurchases. Because premiums generally are collected in advance of claim payments by a period of up to several months, our business normally should produce positive cash flows during periods of increasing premiums and enrollment. Conversely, cash flows would be negatively impacted during periods of decreasing premiums and enrollment. From period to period, our cash flows may also be affected by the timing of working capital items including premiums receivable, benefits payable, and other receivables and payables. Our cash flows are impacted by the timing of payments to and receipts from CMS associated with Medicare Part D subsidies for which we do not assume risk. The use of cash flows may be limited by regulatory requirements of state departments of insurance (or comparable state regulators) which require, among other items, that our regulated subsidiaries maintain minimum levels of capital and seek approval before paying dividends from the subsidiaries to the parent. Our use of cash flows derived from our non-insurance subsidiaries, such as in our Healthcare Services segment, is generally not restricted by state departments of insurance (or comparable state regulators).

For additional information on our liquidity risk, please refer to the section entitled “Risk Factors” in our 2018 Form 10-K.

Cash and cash equivalents increased to approximately $5.5 billion at September 30, 2019 from $2.3 billion at December 31, 2018. The change in cash and cash equivalents for the nine months ended September 30, 2019 and 2018 is summarized as follows:

| | Nine Months Ended | |
|---|---|---|
| | 2019 | 2018 |
| | (in millions) | |
| Net cash provided by operating activities | $ 4,772 | $ 2,506 |
| Net cash used in investing activities | (477) | (2,640) |
| Net cash (used in) provided by financing activities | (1,111) | 234 |
| Increase in cash and cash equivalents | $ 3,184 | $ 100 |

***Cash Flow from Operating Activities***

Our operating cash flow for the 2019 period reflects the significant impact of increasing premiums and enrollment, as premiums generally are collected in advance of claim payments by a period of up to several months. Our operating cash flow for the 2019 period further improved from the 2018 period from the timing of working capital changes, higher earnings, and the impact of an approximately $245 million payment related to reinsuring certain voluntary benefit and financial protection products to a third party in connection with the sale of KMG in 2018.

The most significant drivers of changes in our working capital are typically the timing of payments of benefits expense and receipts for premiums. We illustrate these changes with the following summaries of benefits payable and receivables.

The detail of benefits payable was as follows at September 30, 2019 and December 31, 2018:

| | September 30, 2019 | December 31, 2018 | 2019 Period Change | 2018 Period Change |
|---|---|---|---|---|
| | | (in millions) | | |
| IBNR (1) | $ 4,017 | $ 3,361 | $ 656 | $ 145 |
| Reported claims in process (2) | 1,084 | 617 | 467 | 169 |
| Other benefits payable (3) | 1,119 | 884 | 235 | 38 |
| Total benefits payable | $ 6,220 | $ 4,862 | $ 1,358 | $ 352 |
| Payables from divestiture | | | — | 58 |
| Change in benefits payable per cash flow statement resulting in cash from operations | | | $ 1,358 | $ 410 |

(1) IBNR represents an estimate of benefits payable for claims incurred but not reported (IBNR) at the balance sheet date and includes unprocessed claim inventories. The level of IBNR is primarily impacted by membership levels, medical claim trends and the receipt cycle time, which represents the length of time between when a claim is initially incurred and when the claim form is received and processed (i.e. a shorter time span results in a lower IBNR). IBNR includes unprocessed claims inventories.

(2) Reported claims in process represents the estimated valuation of processed claims that are in the post claim adjudication process, which consists of administrative functions such as audit and check batching and handling, as well as amounts owed to our pharmacy benefit administrator which fluctuate due to bi-weekly payments and the month-end cutoff.

(3) Other benefits payable primarily include amounts owed to providers under capitated and risk sharing arrangements.

The increase in benefits payable from December 31, 2018 to September 30, 2019 and from December 31, 2017 to September 30, 2018 primarily was due to an increase in IBNR primarily as a result of Medicare Advantage membership growth, as well as an increase in the amount of processed but unpaid claims which fluctuate due to month-end cutoff. The increase in benefits payable from December 31, 2018 to September 30, 2019 was also impacted by an increase in the amounts owed to providers under the capitated and risk sharing arrangements.

The detail of total net receivables was as follows at September 30, 2019 and December 31, 2018:

| | September 30, 2019 | December 31, 2018 | 2019 Period Change | 2018 Period Change |
|---|---|---|---|---|
| | (in millions) | | | |
| Medicare | $ 638 | $ 836 | $ (198) | $ 233 |
| Commercial and other | 152 | 135 | 17 | 19 |
| Military services | 131 | 123 | 8 | (48) |
| Allowance for doubtful accounts | (73) | (79) | 6 | 4 |
| Total net receivables | $ 848 | $ 1,015 | $ (167) | $ 208 |
| Reconciliation to cash flow statement: | | | | |
| Receivables from acquisition of business | | | (12) | 3 |
| Change in receivables per cash flow statement resulting in cash from operations | | | $ (179) | $ 211 |

The changes in Medicare receivables for both the 2019 period and the 2018 period reflects the typical pattern caused by the timing of accruals and related collections associated with the CMS risk-adjustment model. Significant collections occur with the mid-year and final settlements with CMS in the second and third quarter.

***Cash Flow from Investing Activities***

Our ongoing capital expenditures primarily relate to our information technology initiatives, support of services in our provider services operations including medical and administrative facility improvements necessary for activities such as the provision of care to members, claims processing, billing and collections, wellness solutions, care coordination, regulatory compliance and customer service. Total capital expenditures, excluding acquisitions, were $506 million in the 2019 period and $436 million in the 2018 period.

Net proceeds from investment securities sales and maturities in the 2019 period were $29 million and $50 million in the 2018 period.

In the third quarter of 2018, we completed the sale of our wholly-owned subsidiary KMG to CGIC. Upon closing, we funded the transaction with approximately $190 million of parent company cash contributed into KMG, subject to customary adjustments, in addition to the transfer of approximately $160 million of statutory capital with the sale. Total cash and cash equivalents, including parent company funding, disposed at September 30, 2018 was $805 million. See Note 3 to our condensed consolidated financial statements.

Also, in the third quarter of 2018, we paid cash consideration of approximately $1.1 billion as part of the Consortium's investment in Kindred, which includes both the Kindred at Home Division and Curo Health Services businesses.

During the 2018 period, we acquired the remaining equity interest in MCCI and acquired FPG for cash consideration of $169 million and $185 million, respectively, as discussed in Note 3 to the condensed consolidated financial statements.

***Cash Flow from Financing Activities***

Receipts from CMS associated with Medicare Part D claim subsidies for which we do not assume risk were higher than claims payments by $113 million in the 2019 period and $436 million in the 2018 period.

Under our administrative services only TRICARE contracts, health care cost payments for which we do not assume risk exceeded reimbursements from the federal government by $102 million in the 2019 period and by $33 million in the 2018 period.

In August 2019, we issued $500 million of 3.125% senior notes due August 15, 2029 and $500 million of 3.950% senior notes due August 15, 2049. Our net proceeds, reduced for the underwriters' discount and commission and offering expenses paid as of September 30, 2019 were $987 million.We used the net proceeds from this offering, together with available cash, to repay the $650 million outstanding amount due under our term note in August 2019, and the $400 million aggregate principal amount of our 2.625% senior notes due on its maturity date of October 1, 2019.

On July 31, 2019, we entered into an accelerated stock repurchase agreement, the July 2019 ASR, with Citibank, N.A., or Citi, to repurchase $1 billion of our common stock. On August 2, 2019, we made a payment of $1 billion to Citi and received an initial delivery of 2.7 million shares of our common stock. See Note 11 to our condensed consolidated financial statements. We expect final settlement under the agreement to occur during the fourth quarter of 2019.

Under a share repurchase plan authorized by the Board of Directors, we repurchased 0.68 million shares during the 2018 period for $224 million. There were no other share repurchases under share repurchase plans authorized by the Board of Directors in the 2019 period with the exception of the July 2019 ASR. We also acquired common shares in connection with employee stock plans for an aggregate cost of $10 million in the 2019 period and $70 million in the 2018 period.

Net repayments of commercial paper were $358 million in the 2019 period and net proceeds from the issuance of commercial paper were $240 million in the 2018 period. The maximum principal amount outstanding at any one time during the 2019 quarter was $670 million.

We paid dividends to stockholders of $216 million during the 2019 period and $195 million during the 2018 period.

**Future Sources and Uses of Liquidity**

***Dividends***

For a detailed discussion of dividends to stockholders, please refer to Note 11 to the condensed consolidated financial statements.

***Stock Repurchases***

For a detailed discussion of stock repurchases, please refer to Note 11 to the condensed consolidated financial statements.

***Debt***

For a detailed discussion of our debt, including our senior notes, credit agreement and commercial paper program, please refer to Note 13 to the condensed consolidated financial statements.

***Acquisitions and Divestitures***

During the 2018 period, we completed the acquisitions of MCCI and FPG for total cash consideration of $354 million. For a detailed discussion of these transactions, please refer to Note 3 to the condensed consolidated financial statements.

***Liquidity Requirements***

We believe our cash balances, investment securities, operating cash flows, and funds available under our credit agreement and our commercial paper program or from other public or private financing sources, taken together, provide adequate resources to fund ongoing operating and regulatory requirements, acquisitions, future expansion opportunities, and capital expenditures for at least the next twelve months, as well as to refinance or repay debt, and repurchase shares.

Adverse changes in our credit rating may increase the rate of interest we pay and may impact the amount of credit available to us in the future. Our investment-grade credit rating at September 30, 2019 was BBB+ according to Standard & Poor's Rating Services, or S&P, and Baa3 according to Moody's Investors Services, Inc., or Moody's. A downgrade by S&P to BB+ or by Moody's to Ba1 triggers an interest rate increase of 25 basis points with respect to $250 million of our senior notes. Successive one notch downgrades increase the interest rate an additional 25 basis points, or annual interest expense by less than $1 million, up to a maximum 100 basis points, or annual interest expense by $3 million.

In addition, we operate as a holding company in a highly regulated industry. Humana Inc., our parent company, is dependent upon dividends and administrative expense reimbursements from our subsidiaries, most of which are subject to regulatory restrictions. We continue to maintain significant levels of aggregate excess statutory capital and surplus in our state-regulated operating subsidiaries. Cash, cash equivalents, and short-term investments at the parent company were $1.7 billion at September 30, 2019 compared to $578 million at December 31, 2018. This increase primarily was due to insurance subsidiary dividends in excess of capital contributions from our parent company as well as operating cash derived from our non-insurance subsidiary earnings, borrowings under senior notes, and other working capital changes. These increases were partially offset by the net repayment of commercial paper borrowings, repayment of short term debt and senior notes, share repurchases, capital expenditures, subsidiaries capital contributions, and cash dividends to shareholders. Our use of operating cash derived from our non-insurance subsidiaries, such as our Healthcare Services segment, is generally not restricted by departments of insurance (or comparable state regulator).

***Regulatory Requirements***

Certain of our subsidiaries operate in states that regulate the payment of dividends, loans, or other cash transfers to Humana Inc., our parent company, and require minimum levels of equity as well as limit investments to approved securities. The amount of dividends that may be paid to Humana Inc. by these subsidiaries, without prior approval by state regulatory authorities, or ordinary dividends, is limited based on the entity's level of statutory income and statutory capital and surplus. If the dividend, together with other dividends paid within the preceding twelve months, exceeds a specified statutory limit or is paid from sources other than earned surplus, it is generally considered an extraordinary dividend requiring prior regulatory approval. In most states, prior notification is provided before paying a dividend even if approval is not required.

Although minimum required levels of equity are largely based on premium volume, product mix, and the quality of assets held, minimum requirements vary significantly at the state level. Based on the most recently filed statutory financial statements as of June 30, 2019, our state regulated subsidiaries had aggregate statutory capital and surplus of approximately $7.6 billion, which exceeded aggregate minimum regulatory requirements of $5.7 billion. The amount of dividends paid to our parent company was approximately $1.4 billion during the nine months ended September 30, 2019 compared to $1.9 billion during the nine months ended September 30, 2018. Actual dividends paid may vary year over year due to consideration of excess statutory capital and surplus and expected future surplus requirements related to, for example, premium volume and product mix.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

Our earnings and financial position are exposed to financial market risk, including those resulting from changes in interest rates.

Interest rate risk also represents a market risk factor affecting our consolidated financial position due to our significant investment portfolio, consisting primarily of fixed maturity securities of investment-grade quality with a weighted average S&P credit rating of AA at September 30, 2019. Our net unrealized position increased $447 million from a net unrealized loss position of $204 million at December 31, 2018 to a net unrealized gain position of $243 million at September 30, 2019. At September 30, 2019, we had gross unrealized losses of $10 million on our investment portfolio primarily due to an increase in market interest rates since the time the securities were purchased. There were no material other-than-temporary impairments during the nine months ended September 30, 2019. While we believe that these impairments are temporary and we currently do not have the intent to sell such securities, given the current market conditions and the significant judgments involved, there is a continuing risk that future declines in fair value may occur and material realized losses from sales or other-than-temporary impairments may be recorded in future periods.

Duration is the time-weighted average of the present value of the bond portfolio’s cash flow. Duration is indicative of the relationship between changes in fair value and changes in interest rates, providing a general indication of the sensitivity of the fair values of our fixed maturity securities to changes in interest rates. However, actual fair values may differ significantly from estimates based on duration. The average duration of our investment portfolio, including cash and cash equivalents, was approximately 2.3 years as of September 30, 2019 and approximately 2.9 years as of December 31, 2018. The decline in the average duration is reflective of the longer duration securities associated with the sale of KMG. Based on the duration, including cash equivalents, a 1% increase in interest rates would generally decrease the fair value of our securities by approximately $356 million at September 30, 2019.

**Item 4. Controls and Procedures**

Under the supervision and with the participation of our Chief Executive Officer, or CEO, our Chief Financial Officer, or CFO, and our Principal Accounting Officer, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures for the quarter ended September 30, 2019.

Based on our evaluation, our CEO, CFO, and our Principal Accounting Officer concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information the Company is required to disclose in its reports under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, including, without limitation, ensuring that such information is accumulated and communicated to the Company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

There have been no changes in the Company’s internal control over financial reporting during the quarter ended September 30, 2019 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

## Part II. Other Information

### Item 1. Legal Proceedings

For a description of the legal proceedings pending against us and certain other pending or threatened litigation, investigations, or other matters, see "Legal Proceedings and Certain Regulatory Matters" in Note 14 to the condensed consolidated financial statements beginning on page 31 of this Form 10-Q.

### Item 1A. Risk Factors

There have been no changes to the risk factors included in our 2018 Form 10-K.

### Item 2: Unregistered Sales of Equity Securities and Use of Proceeds

(a) None.

(b) N/A

(c) The following table provides information about our purchases of equity securities that are registered by us pursuant to Section 12 of the Securities Exchange Act of 1934, as amended, during the three months ended September 30, 2019:

| Period | Total Number of Shares Purchased (1)(2) | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)(2) | Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1) |
|---|---|---|---|---|
| July 2019 | — | $ — | — | $ 3,000,000,000 |
| August 2019 | 2,695,872 | 296.75 | 2,695,872 | 2,000,000,000 |
| September 2019 | — | — | — | 2,000,000,000 |
| Total | 2,695,872 | $ — | 2,695,872 | |

(1) On July 30, 2019, the Board of Directors replaced a previous share repurchase authorization of up to $3 billion (of which approximately $1.03 billion remained unused) with a new authorization for repurchases of up to $3 billion of our common shares exclusive of shares repurchased in connection with employee stock plans, expiring on June 30, 2022. On July 31, 2019, we entered into an accelerated stock repurchase agreement, the July 2019 ASR, with Citibank, N.A., or Citi, to repurchase $1 billion of our common stock. On August 2, 2019, we made a payment of $1 billion to Citi and received an initial delivery of 2.7 million shares of our common stock. We recorded the payment to Citi as a reduction to stockholders' equity, consisting of an $800 million increase in treasury stock, which reflects the value of the initial 2.7 million shares received upon initial settlement, and a $200 million decrease in capital in excess of par value, which reflects the value of stock held back by Citi pending final settlement of the agreement. The final number of shares that we may receive, or be required to remit, under the agreement, will be determined based on the daily volume-weighted average share price of our common stock over the term of the July 2019 ASR, less a discount and subject to adjustments pursuant to the terms and conditions of the July 2019 ASR. We expect final settlement under the July 2019 ASR to occur during the fourth quarter of 2019.

(2) Excludes 35,000 shares repurchased in connection with employee stock plans.

### Item 3: Defaults Upon Senior Securities

None.

**Item 4: Mine Safety Disclosures**

Not applicable.

**Item 5: Other Information**

None.

**Item 6: Exhibits**

| | |
|---|---|
| 3(i) | Restated Certificate of Incorporation of Humana Inc. filed with the Secretary of State of Delaware on November 9, 1989, as restated to incorporate the amendment of January 9, 1992, and the correction of March 23, 1992 (incorporated herein by reference to Exhibit 4(i) to Humana Inc.'s Post-Effective Amendment No. 1 to the Registration Statement on Form S-8 (Reg. No. 33-49305) filed February 2, 1994). |
| 3(ii) | By-Laws of Humana Inc., as amended on December 14, 2017 (incorporated herein by reference to Exhibit 3(b) to Humana Inc.'s Current Report on Form 8-K, filed December 14, 2017). |
| 10.1 | Amended and Restated Humana Inc. Executive Incentive Compensation Plan, effective January 1, 2020. |
| 31.1 | Principal Executive Officer certification pursuant to Section 302 of Sarbanes–Oxley Act of 2002. |
| 31.2 | Principal Financial Officer certification pursuant to Section 302 of Sarbanes–Oxley Act of 2002. |
| 32 | Principal Executive Officer and Principal Financial Officer certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101 | The following materials from Humana Inc.'s Quarterly Report on Form 10-Q formatted in iXBRL (Inline Extensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets at September 30, 2019 and December 31, 2018; (ii) the Condensed Consolidated Statements of Income for the three and nine months ended September 30, 2019 and 2018; (iii) the Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2019 and 2018; (iv) the Consolidated Statements of Equity for the three and nine months ended September 30, 2019 and 2018; (v) the Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2019 and 2018; and (vi) Notes to Condensed Consolidated Financial Statements. The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document. |
| 104 | Cover Page Interactive Data File formatted in Inline XBRL and contained in Exhibit 101. |

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HUMANA INC.
(Registrant)

| | | | |
|---|---|---|---|
| Date: | November 6, 2019 | By: | /s/ CYNTHIA H. ZIPPERLE |
| | | | Cynthia H. Zipperle |
| | | | Senior Vice President, Chief Accounting Officer and Controller (Principal Accounting Officer) |

**Exhibit 10.1**

**HUMANA INC.**
**EXECUTIVE INCENTIVE COMPENSATION PLAN**
**As Amended and Restated January 1, 2020**

## I. OBJECTIVES:

The objectives of the Humana Inc. Executive Management Incentive Compensation Plan, as amended and restated (the "Plan") are to (i) link the compensation of selected executives to certain key performance targets; and (ii) reward them, when appropriate, for their efforts in achieving the performance targets of Humana Inc. (the "Company"), consistent with appropriate balance of risk and reward and appropriate risk management practices aligned to the Company's short-term and long-term strategic plan.

## II. ELIGIBILITY AND AWARDS:

**a.** Executives participating in this Plan ("Participants") will be limited to Section 16 officers of Humana Inc., as determined pursuant to Section 16 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Participation in the Plan will be approved by the Organization & Compensation Committee of the Board of Directors of the Company (the "Committee"). Each Participant shall be notified of his/her selection as a Participant.

**b.** Incentive compensation will be computed by measuring the Company's achievement of predetermined goals ("Performance Targets") established by the Committee in accordance with Internal Revenue Service regulations promulgated under Section 162(m) of the Internal Revenue Code as amended (the "Code"), to the extent applicable. Performance Targets may be expressed in terms of (i) earnings per share, (ii) share price or total shareholder return, (iii) consolidated net income, (iv) pre-tax profits, (v) earnings or net earnings, (vi) return on equity or assets, (vii) sales, (viii) cash flow from operating activities, (ix) return on invested capital, (x) membership, (xi) other performance objectives as determined by the Committee, to the extent permitted under Section 162(m) of the Code (if applicable), or (xii) any combination of the foregoing. Performance Targets may be in respect of the performance of the Company, any of its Subsidiaries, any of its divisions or any combination thereof. Performance Targets may be absolute or relative (to prior performance of the Company or to the performance of one or more other entities or external indices) and may be expressed in terms of a progression within a specified range.

**c.** Incentive compensation for a fiscal year or other relevant period determined by the Committee ("Performance Period") shall be based on the Participant's base salary paid or accrued during such fiscal year exclusive of any bonus, equity compensation, or fringe benefits paid or accrued during such fiscal year ("Salary"). The Committee shall determine, subject to the limits in the Plan, the potential percentage of Salary which any Participant shall be eligible to receive as incentive compensation, which need not be the same for each Participant. The precise percentage earned shall be based upon a schedule of achievement of Performance Targets. Notwithstanding anything herein to the contrary, the maximum incentive compensation paid for any fiscal year to the CEO may not exceed Six Million Dollars ($6,000,000), or Three Million Dollars ($3,000,000) for any other Participant.

**d.** The Company's achievement of any relevant Performance Targets will be determined in accordance with generally accepted accounting principles. Any incentive compensation generated pursuant to incentive plans of the Company, including this Plan, shall be accrued and deducted as an expense in the appropriate fiscal year in determining the achievement of any Performance Targets.

**e.** Each Participant may receive an award ("Award") if the Performance Target(s) established by the Committee are attained in the applicable Performance Period. The applicable Performance Period and Performance Target(s) shall be determined by the Committee consistent with the terms of the Plan and, to the extent applicable, Section 162(m) of the Code. Notwithstanding the fact that the Performance Target(s) have been attained, the Committee may pay an Award of less than the amount determined by the formula or standard established by the Committee or may pay no Award at all.

**f.** The specific Performance Target(s) must be established by the Committee in advance of the deadlines applicable under Section162(m) of the Code, to the extent applicable, and while the performance relating to the Performance Target(s) remains substantially uncertain within the meaning of Section162(m) of the Code. The Performance Target(s) with respect to any Performance Period may be established on a cumulative basis or in the alternative, and may be established on a stand-alone basis with respect to the Company or on a relative basis with respect to any peer companies or index selected by the Committee. At the time the Performance Target(s) are selected, the Committee shall provide, in terms of an objective formula or standard for each Participant, the method of computing the specific amount of Award payable to the Participant if the Performance Target(s) are attained. The objective formula or standard shall preclude the use of discretion to increase the amount of any Award earned pursuant to the terms of the Award.

**g.** If services as a Participant commence after the adoption of the Plan and the Performance Target(s) are established for a Performance Period, the Committee may grant an Award that is proportionately adjusted based on the period of actual service, and the amount of any Award paid to such Participant shall not exceed that proportionate amount of the applicable maximum individual Award allowable under the Plan.

**h.** Notwithstanding anything to the contrary set forth herein, the Performance Target(s) shall be adjusted to reflect the following events resulting in a change to the applicable Performance Target in excess of the aggregate threshold amount established by the Committee at the time of the applicable performance period:

**i.** the acquisition or disposition of a business, a merger, or a similar transaction, and the related integration costs including external costs such as legal, accounting and consulting fees and internal costs such as severance and benefits, contract cancellation costs, lease abandonment costs, overhead costs of integration including allocated wages and benefits and administrative costs in connection therewith;

**ii.** the impact of securities issuances or repurchases in connection with an acquisition or disposition of a business, a merger, or a similar transaction, and related expenses including both direct and incremental costs incurred in connection therewith

**iii.** changes in accounting principles, tax laws, or other laws, provisions or regulation

**iv.** any litigation or regulatory investigations not in the ordinary course of business

**v.** the impact of impairment of tangible or intangible assets; including goodwill

**vi.** the impact of restructuring or business recharacterization activities, including but not limited to reductions in force, that are reported publicly by the Company

**vii.** the impact of investments or acquisitions made during the year or, to the extent provided by the Committee, any prior year

**i.** To preserve the intended incentives and benefits of an Award based on a Performance Target, the Committee may determine at the time Performance Targets are established that certain adjustments shall apply to the objective formula or standard with respect to the applicable Performance Target to take into account, in whole or in part, in any manner specified by the Committee, any one or more of the following with respect to the Performance Period: (i)the gain, loss, income or expense resulting from changes in accounting principles that become effective during the Performance Period; (ii)the gain, loss, income or expense reported publicly by the Company with respect to the Performance Period that are extraordinary or unusual in nature or infrequent in occurrence; (iii)the gains or losses resulting from, and the direct expenses incurred in connection with the disposition of a business, or the sale of investments or non-core assets; (iv)the gain or loss from all or certain claims and/or litigation and all or certain insurance recoveries relating to claims or litigation;(v)the impact of impairment of tangible or intangible assets; including goodwill; (vi)the impact of restructuring or business recharacterization activities, including but not limited to reductions in force, that are reported publicly by the Company; or (vii)the impact of investments or acquisitions made during the year or, to the extent provided by the Committee, any prior year. Each of the adjustments described in this Section may relate to the Company as a whole or any part of the Company's business operations. The adjustments are to be determined in accordance with generally accepted accounting principles and standards, unless another objective method of measurement is designated by the Committee.

**j.** The Committee has the sole discretion to determine the standard or formula pursuant to which each Participant's Award shall be calculated and whether all or any portion of the amount so calculated will be paid, subject in all cases to the terms, conditions and limits of the Plan. To this same extent, the Committee may at any time establish (and, once established, rescind, waive or amend) additional conditions and terms of payment of Awards (including but not limited to the achievement of other financial, strategic or individual goals, which may be objective or subjective) as it may deem desirable in carrying out the purposes of the Plan and may take into account such other factors as it deems appropriate in administering any aspect of the Plan. The Committee may not, however, increase the maximum amount permitted to be paid to any individual under the Plan or pay Awards under this Plan if applicable Performance Target(s) have not been satisfied.

**k.** Incentive compensation shall be paid to Participants on or before March 15th of the year following the fiscal year with respect to which it was earned or such earlier date as may be required in order that such amount be deductible under the Code for the fiscal year with respect to which it was earned.

**III. ADMINSTRATION OF THIS PLAN:**

The Committee has sole authority (except as specified otherwise herein) to determine all questions of interpretation and application of the Plan, or of the terms and conditions pursuant to which Awards are granted under the Plan and in general, to make all determinations advisable for the administration of the Plan to achieve its purpose. The Committee determinations under the Plan (including without limitation, determinations of the persons to receive Awards, the form, amount and timing of such Awards, the terms and provisions of such Awards and any agreements evidencing such Awards) need not be uniform and may be made by the Committee selectively among persons who receive or are eligible to receive Awards under the Plan, whether or not such persons are similarly situated. Such determination shall be final and not subject to further appeal.

**IV. TERMINATION OF EMPLOYMENT:**

Subject to the discretion of the Committee, a Participant must be actively employed or on short-term disability (as determined pursuant to the applicable company policy on the last day of the applicable Performance Period to be eligible for a payout, unless the Participant's employment was terminated due to the:

**a.** The Participant's death or [Disability (as defined in the Amended and Restated Humana Inc. Stock Incentive Plan

**b.** The Participant's Retirement

**c.** The Participant's termination of employment due to a(A) Workforce Reduction, (B) Position Elimination, (C) Divestiture or(D) position reassignment to a Strategic Joint Venture (as each term is defined in the Amended and Restated Humana Inc. Stock Incentive Plan)

To the extent that a Participant is not actively employed on the last day of the applicable Performance Period due to death, Disability, Retirement, Workforce Reduction, Position Elimination, Divestiture or position reassignment to a Strategic Joint Venture, the Participant will be eligible to receive a pro-rated Award based on the period that the Participant was actively employed during the Performance Period, with the amount of the pro-rated Award to be based on actual performance and paid at the same time as Awards are paid to employees who remain actively employed through the end of the applicable Performance Period.

**V. AMENDMENT OF PLAN:**

Subject to any restrictions imposed under Section 162(m) of the Code, to the extent applicable, the Committee may at any time and from time to time alter, amend, suspend or terminate the Plan in whole or in part, provided that no such amendment that would require the consent of the Board and/or stockholders of the Company pursuant to Section 162(m) of the Code, to the extent applicable, or the Exchange Act, any New York Stock Exchange (or other relevant stock exchange) rule or regulation, or any other applicable law, rule or regulation, shall be effective without such consent.

## VI. GENERAL PROVISIONS:

**a.** No person has any claim or right to be included in this Plan or to be granted incentive compensation under this Plan until such individual has been declared a Participant and received official notice thereof in accordance with the procedures as set forth in this Plan. In addition, all of the requirements and applicable rules and regulations of this Plan must have been met including, but not limited to the availability of funds for incentive compensation awards and the determination by the Committee of the extent to which Performance Targets have been met.

**b.** The designation of an individual as a Participant under this Plan does not in any way alter the nature of the Participant's employment relationship. Participation in this Plan shall not constitute a contract of employment between the Company or any subsidiary and any person and shall not be deemed to be consideration for, or a condition of, continued employment of any person.

**c.** No benefit provided under the Plan shall be subject to alienation or assignment by a Participant (or by any person entitled to such benefit pursuant to the terms of this Plan), nor shall it be subject to attachment or other legal process except (i) to the extent specifically mandated and directed by applicable state or federal statute; and (ii) as requested by the Participant and approved by the Committee to members of the Participant's family, or a trust established by the Participant for the benefit of family members.

**d.** The Company or a subsidiary may withhold any applicable federal, state or local taxes at such time and upon such terms and conditions as required by law or determined by the Company or subsidiary.

**e.** Each member of the Committee (and each person to whom the Committee or any member thereof has delegated any of its authority or power under this Plan) shall be fully justified in relying or acting in good faith upon any report made by the independent public accountants of the Company and its subsidiaries and upon any other information furnished the Committee in connection with the Plan. In no event shall any person who is or shall have been a member of the Committee be liable for any determination made or other action taken or any omission to act in reliance upon any such report or information, or for any action taken or failure to act if in good faith.

**f.** In the event the Company becomes a party to a merger, consolidation, sale of substantially all of its assets or any other corporate reorganization in which the Company will not be the surviving corporation or in which the holders of the common stock of the Company will receive securities of another corporation (in any such case, the "New Company"), then the New Company shall assume the rights and obligations of the Company under this Plan.

**g.** All matters relating to the Plan or to Awards granted hereunder shall be governed by the laws of the State of Delaware, without regard to the principles of conflict of laws.

**h.** The expenses of administering the Plan shall be borne by the Company and its subsidiaries.

**i.** The titles and headings of the sections in the Plan are for convenience of reference only, and in the event of any conflict, the text of the Plan, rather than such titles or headings, shall control.

## VII. STOCKHOLDER APPROVAL

This Plan has been previously approved by the Company's stockholders at the April 24, 2008 annual meeting of stockholders.

## VIII. INTERNAL REVENUE CODE SECTION 162(m):

Transactions under this Plan are intended to comply with all applicable conditions of Section 162(m) of the Internal Revenue Code, as amended, or its successor. To the extent any provision of the Plan or action by the Committee fails to so comply, to the extent applicable, it shall be deemed null and void, to the extent permitted by law and deemed advisable by the Committee.

## IX. INTERNAL REVENUE CODE SECTION 409A

All Awards granted under the Plan are intended to be exempt from Section 409A of the Code. Notwithstanding this or any other provision of the Plan to the contrary, the Committee may amend the

Plan or any Award granted hereunder in any manner, or take any other action that it determines, in its sole discretion, is necessary, appropriate or advisable (including replacing any Award) to cause the Plan or any Award granted hereunder to not be subject to Section 409A of the Code. Any such action, once taken, shall be deemed to be effective from the earliest date necessary to avoid a violation of Section 409A of the Code and shall be final, binding and conclusive on all Participants and other individuals having or claiming any right or interest under the Plan.

**Exhibit 31.1**

**CERTIFICATION PURSUANT TO SECTION 302 OF SARBANES-OXLEY ACT OF 2002**

I, Bruce D. Broussard, principal executive officer of Humana Inc., certify that:

1. I have reviewed this Quarterly Report of Humana Inc. (the “Company”) on Form 10-Q for the period ending September 30, 2019;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of the annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

| | |
|---|---|
| Date: | November 6, 2019 |
| Signature: | /s/ Bruce D. Broussard |
| | Bruce D. Broussard<br>Principal Executive Officer |

**Exhibit 31.2**

**CERTIFICATION PURSUANT TO SECTION 302 OF SARBANES-OXLEY ACT OF 2002**

I, Brian A. Kane, principal financial officer of Humana Inc., certify that:

1. I have reviewed this Quarterly Report of Humana Inc. (the “Company”) on Form 10-Q for the period ending September 30, 2019;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of the annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

| | |
|---|---|
| Date: | November 6, 2019 |
| Signature: | /s/ Brian A. Kane |
| | Brian A. Kane<br>Principal Financial Officer |

**Exhibit 32**

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED**

**PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Humana Inc. (the “Company”) on Form 10-Q for the period ending September 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), each of the undersigned hereby certifies, pursuant to 18 U.S.C. Sec. 1350, as adopted pursuant to Sec. 906 of the Sarbanes-Oxley Act of 2002, in his capacity as an officer of Humana Inc., that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Bruce D. Broussard

Bruce D. Broussard
Principal Executive Officer

November 6, 2019

/s/ Brian A. Kane

Brian A. Kane
Principal Financial Officer

November 6, 2019

A signed original of this written statement required by Section 906 has been provided to Humana Inc. and will be retained by Humana Inc. and furnished to the Securities and Exchange Commission or its staff upon request.