GALLAGHER ARTHUR J & CO
Form 10-K
February 08, 2019
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended December 31, 2018

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 1-09761

ARTHUR J. GALLAGHER & CO.

(Exact name of registrant as specified in its charter)

DELAWARE	**36-2151613**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
2850 Golf Road	
Rolling Meadows, Illinois	**60008-4050**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code (630) 773-3800

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

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

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

None

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

Act. Yes No .

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

Act. Yes No .

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See 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 Exchange Act). Yes No .

The aggregate market value of the voting common equity held by non-affiliates of the registrant, computed by reference to the last reported price at which the registrant s common equity was sold on June 30, 2018 (the last day of the registrant s most recently completed second quarter) was $10,435,000.

The number of outstanding shares of the registrant s Common Stock, $1.00 par value, as of January 31, 2019 was 184,060,000.

Documents incorporated by reference: Portions of Arthur J. Gallagher & Co. s definitive 2019 Proxy Statement are incorporated by reference into this Form 10-K in response to Part III to the extent described herein.

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Information Concerning Forward-Looking Statements

This report contains certain statements related to future results, or states our intentions, beliefs and expectations or predictions for the future, which are forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements relate to expectations or forecasts of future events. Such statements use words such as anticipate, believe, estimate, expect, contemplate, forecast, project, intend, plan, potential, and other similar terms, and future or conditional tense verbs like could, may, should, will and would. You can also identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. For example, we may use forward-looking statements when addressing topics such as: market and industry conditions, including competitive and pricing trends; acquisition strategy; the expected impact of acquisitions and dispositions; the development and performance of our services and products; changes in the composition or level of our revenues or earnings; future debt levels and anticipated actions to be taken in connection with maturing debt; future debt to earnings ratios; the outcome of contingencies; dividend policy; pension obligations; cash flow and liquidity; capital structure and financial losses; future actions by regulators; the outcome of existing regulatory actions, investigations, reviews or litigation; the impact of changes in accounting rules, including the new revenue recognition and lease accounting standards; financial markets; interest rates; foreign exchange rates; matters relating to our operations; income taxes, including the impact of tax reform; and expectations regarding our investments, including our clean energy investments. These forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from either historical or anticipated results depending on a variety of factors.

Potential factors that could impact results include:

- Failure to successfully and cost-effectively integrate recently acquired businesses and their operations or fully realize synergies from such acquisitions in the expected time frame;

- Volatility or declines in premiums or other adverse trends in the insurance industry;

- An economic downturn or unstable economic conditions, whatever the cause, including Brexit, a prolonged shutdown of the U.S. government and trade wars;

- Competitive pressures in each of our businesses;

- Risks that could negatively affect the success of our acquisition strategy, including continuing consolidation in our industry and growing interest in acquiring insurance brokers on the part of private equity firms, which could make it more difficult to identify targets and could make them more expensive; the risk that we may not receive timely regulatory approval of desired transactions; execution risks; integration risks; the risk of post-acquisition deterioration leading to intangible asset impairment charges; and the risk we could incur or assume unanticipated liabilities such as cybersecurity issues or those relating to violations of anti-corruption and sanctions laws;

- Risks arising from changes in U.S. or foreign tax laws, including our ability to effectively implement and account for the U.S. Tax Cuts and Jobs Act (which we refer to as the Tax Act);

- Our failure to attract and retain experienced and qualified talent, including our senior management team;

- Risks arising from our substantial international operations, including the risks posed by political and economic uncertainty in certain countries (such as the risks posed by Brexit), risks related to maintaining regulatory and legal compliance across multiple jurisdictions (such as those relating to violations of anti-corruption, sanctions and privacy laws), and risks arising from the complexity of managing businesses across different time zones, languages, geographies, cultures and legal regimes that conflict with one another at times;

Risks particular to our risk management segment, including any slowing of the trend toward outsourcing claims administration, and of the concentration of large amounts of revenue with certain clients;

The higher level of variability inherent in contingent and supplemental revenues versus standard commission revenues, particularly in light of the new revenue recognition accounting standard;

Sustained increases in the cost of employee benefits;

Our failure to apply technology effectively in driving value for our clients through technology-based solutions, or failure to gain internal efficiencies and effective internal controls through the application of technology and related tools;

A disaster or other significant disruption to business continuity;

Damage to our reputation;

Our failure to comply with regulatory requirements, including those related to governance and control requirements in particular jurisdictions, international sanctions, or a change in regulations or enforcement policies that adversely affects our operations (for example, relating to insurance broker compensation methods or the failure of state and local governments to follow through on agreed-upon income tax credits or other tax related incentives, relating to our corporate headquarters);

Violations or alleged violations of the U.S. Foreign Corrupt Practices Act (which we refer to as FCPA), the U.K. Bribery Act 2010 or other anti-corruption laws and the Foreign Account Tax Compliance provisions of the Hiring Incentives to Restore Employment Act (which we refer to as FATCA);

The outcome of any existing or future investigation, review, regulatory action or litigation;

- Unfavorable determinations related to contingencies and legal proceedings;
- Cyber attacks or other cybersecurity incidents; improper disclosure of confidential, personal or proprietary data; and changes to laws and regulations governing cybersecurity and data privacy;
- Significant changes in foreign exchange rates;
- Changes to our financial presentation from new accounting estimates and assumptions (including as a result of the new lease and revenue recognition standards or the Tax Act);
- Risks related to our clean energy investments, including the risk of intellectual property claims, utilities switching from coal to natural gas or other renewable energy sources, environmental and product liability claims, environmental compliance costs and the risk of disallowance by the Internal Revenue Service (which we refer to as IRS) of previously claimed tax credits;
- The risk that our outstanding debt adversely affects our financial flexibility and restrictions and limitations in the agreements and instruments governing our debt;
- The risk we may not be able to receive dividends or other distributions from subsidiaries;
- The risk of share ownership dilution when we issue common stock as consideration for acquisitions and for other reasons; and
- Volatility of the price of our common stock.

Forward-looking statements are not guarantees of future performance. They involve risks, uncertainties and assumptions, including the risk factors referred to above. Our future performance and actual results may differ materially from those expressed in forward-looking statements. Accordingly, you should not place undue reliance on forward-looking statements, which speak only as of, and are based on information available to us on, the date of the applicable document. Many of the factors that will determine these results are beyond our ability to control or predict. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Forward-looking statements speak only as of the date that they are made, and we do not undertake any obligation to update any such statements or release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date of this report or to reflect new information, future or unexpected events or otherwise, except as required by applicable law or regulation. Further information about factors that could materially affect us, including our results of operations and financial condition, is contained in the Risk Factors section in Part I, Item 1A of this report.

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Arthur J. Gallagher & Co.

Annual Report on Form 10-K

For the Fiscal Year Ended December 31, 2018

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Part I

Item 1. Business.

Overview

Arthur J. Gallagher & Co. and its subsidiaries, collectively referred to herein as we, our, us or Gallagher, are engaged in providing insurance brokerage, consulting, and third-party property/casualty claims settlement and administration services to businesses and organizations around the world. We believe that our major strength is our ability to deliver comprehensively structured insurance, insurance and risk management solutions, superior claim outcomes and comprehensive consulting services to our clients.

Our brokerage segment operations provide brokerage and consulting services to businesses and organizations of all types, including commercial, not-for-profit, and public entities, and, to a lesser extent, individuals, in the areas of insurance placement, risk of loss management, and management of employer sponsored benefit programs. Our risk management segment operations provide contract claim settlement, claim administration, loss control services and risk management consulting for commercial, not-for-profit, captive and public entities, and various other organizations that choose to self-insure property/casualty coverages or choose to use a third-party claims management organization rather than the claim services provided by an underwriting enterprise.

We do not assume underwriting risk on a net basis, other than with respect to de minimis amounts necessary to provide minimum or regulatory capital to organize captives, pools, specialized underwriters or risk-retention groups. Rather, capital necessary for covering events of loss is provided by underwriting enterprises, which we define as insurance companies, reinsurance companies and various other risk-taking entities, including intermediaries of underwriting enterprises, that we do not own or control.

Since our founding in 1927, we have grown from a one-person insurance agency to the world s fourth largest insurance broker/risk manager based on revenues, according to *Business Insurance* magazine s July 2018 edition, and one of the world s largest property/casualty third party claims administrators, according to *Business Insurance* magazine s May 2018 edition. We have three reportable segments: brokerage, risk management and corporate, which contributed approximately 61%, 14% and 25%, respectively, to 2018 revenues. We generate approximately 70% of our revenues from the combined brokerage and risk management segments in the United States (U.S.), with the remaining 30% derived internationally, primarily in Australia, Bermuda, Canada, the Caribbean, New Zealand and the United Kingdom (U.K.). All of the revenues of the corporate segment are generated in the U.S.

Shares of our common stock are traded on the New York Stock Exchange under the symbol AJG , and we had a market capitalization at December 31, 2018 of approximately $13.6 billion. Information in this report is as of December 31, 2018 unless otherwise noted. We were reincorporated as a Delaware corporation in 1972. Our executive offices are located at 2850 Golf Road, Rolling Meadows, Illinois 60008-4050, and our telephone number is (630) 773-3800.

Operating Segments

We report our results in three segments: brokerage, risk management and corporate. The major sources of our operating revenues are commissions, fees and supplemental and contingent revenues from our brokerage operations, and fees, including performance-based fees, from our risk management operations. The corporate segment generates revenues from our clean energy investments

Our business, particularly our brokerage business, is subject to seasonal fluctuations. Commissions, fees, supplemental revenues and contingent revenues, and our costs to obtain and fulfill the service obligations to our clients, can vary from quarter to quarter as a result of the timing of contract-effective dates. On the other hand, salaries and employee benefits, rent, depreciation and amortization expenses generally tend to be more uniform throughout the year. The timing of acquisitions, recognition of books of business gains and losses and the variability in the recognition of tax credits generated by our clean energy investments also impact the trends in our quarterly operating results. See Note 20 to our 2018 consolidated financial statements for unaudited quarterly operating results for 2018 and 2017.

Brokerage Segment

The brokerage segment accounted for 61% of our revenues in 2018. We operate our brokerage segment operations through a network of more than 590 sales and service offices located throughout the U.S. and another 277 sales and service offices in 35 countries, but most of which are in Australia, Canada, the Caribbean, New Zealand and the U.K. Most of these offices are fully staffed with sales and service personnel. We also offer client service capabilities in more than 150 countries around the world through a network of correspondent brokers and consultants.

Our brokerage segment generates revenues by:

(i) Identifying, negotiating and placing all forms of insurance or reinsurance coverages, as well as providing risk-shifting, risk-sharing and risk-mitigation consulting services, principally related to property/casualty, life, health, welfare and disability insurance. We also provide these services through, or in conjunction with, other unrelated agents and brokers, consultants and management advisors.

(ii) Acting as an agent or broker for multiple underwriting enterprises by providing services such as sales, marketing, selecting, negotiating, underwriting, servicing and placing insurance coverage on their behalf.

(iii) Providing consulting services related to health and welfare benefits, voluntary benefits, executive benefits, compensation, retirement planning, institutional investment and fiduciary, actuarial, compliance, private insurance exchange, human resource technology, communications and benefit administration.

(iv) Providing management and administrative services to captives, pools, risk-retention groups, healthcare exchanges, small underwriting enterprises, such as accounting, claims and loss processing assistance, feasibility studies, actuarial studies, data analytics and other administrative services.

The vast majority of our brokerage contracts and service understandings are for a period of one year or less.

Commissions and fees

The primary source of brokerage segment revenues is commissions from underwriting enterprises, which are based on a percentage of premiums paid by our clients, or fees received from clients based on an agreed level of service usually in lieu of commissions.

Commissions are fixed at the contract effective date and generally are based on a percentage of premium for insurance coverage or employee head count for employer sponsored benefit plans. Commissions depend upon a large number of factors, including the type of risk being placed, the particular underwriting enterprise s demand, the expected loss experience of the particular risk of coverage, and historical benchmarks surrounding the level of effort necessary for us to place and service the insurance contract. Rather than being tied to the amount of premiums, fees are typically based on an expected level of effort to provide our services.

Whether we are paid a commission or a fee, the vast majority of our services are associated with the placement of an insurance (or insurance-like) contract. See Revenue Recognition in Note 1 to our 2018 consolidated financial statements. See Note 2 to our 2018 consolidated financial statements for information with respect to the impacts that a new accounting standard, relating to revenue recognition, had on our financial position and operating results.

Supplemental revenues

Certain underwriting enterprises may pay us additional revenues based on the volume of premium we place with them and for insights into our sales pipeline, our sales capabilities or our risk selection knowledge. These amounts are in excess of the commission and fee revenues discussed above, and not all business we place with underwriting enterprises is eligible for supplemental revenues. See Revenue Recognition in Note 1 to our 2018 consolidated financial statements. See Note 2 to our 2018 consolidated financial statements for information with respect to the impacts that a new accounting standard, relating to revenue recognition, had on our financial position and operating results.

Contingent revenues

Certain underwriting enterprises may pay us additional revenues for our sales capabilities, our risk selection knowledge, or our administrative efficiencies. These amounts are in excess of the commission revenues discussed above, and not all business we place with participating underwriting enterprises is eligible for contingent revenues. Unlike supplemental revenues, also discussed above, these revenues are variable, generally based on growth, the loss experience of the underlying insurance contracts, and/or our efficiency in processing the business. See Revenue Recognition in Note 1 to our 2018 consolidated financial statements. See Note 2 to our 2018 consolidated financial statements for information with respect to the impacts that a new accounting standard, relating to revenue recognition, had on our financial position and operating results.

Sub-brokerage costs

Sub-brokerage costs are excluded from our gross revenues in our determination of our total revenues. Sub-brokerage costs represent commissions paid to sub-brokers related to the placement of certain business by our brokerage segment operations. We recognize this contra revenue in the same manner as the commission revenue to which it relates.

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Retail Insurance Brokerage Operations

Our retail insurance brokerage operations accounted for 84% of our brokerage segment revenues in 2018. Our retail brokerage operations place nearly all lines of commercial property/casualty and health and welfare insurance coverage. Significant lines of insurance coverage and consultant capabilities are as follows:

Aviation	Disability	General Liability	Products Liability
Casualty	Earthquake	Health & Welfare	Professional Liability
Claims Advocacy	Errors & Omissions	Healthcare Analytics	Property
Commercial Auto	Exchange Solutions	Human Resources	Retirement
Compensation	Executive Benefits	Institutional Investment	Surety Bond
Cyber Liability	Fiduciary Services	Loss Control	Voluntary Benefits
Dental	Fine Arts	Marine	Wind
Directors & Officers Liability	Fire	Medical	Workers Compensation

Our retail brokerage operations are organized and operate within certain key niche/practice groups, which account for approximately 73% of our retail brokerage revenues. These specialized teams target areas of business and/or industries in which we have developed a depth of expertise and a large client base. Significant niche/practice groups we serve are as follows:

Affinity	Equity Advisors	Law Firms	Real Estate/Hospitality
Automotive	Financial Institutions	Life Sciences	Religious
Aviation	Food/Agribusiness	Marine	Restaurant
Construction	Global Risks	Not-for-Profit	Technology
Energy	Healthcare	Personal	Trade Credit/Political Risk
Entertainment	Higher Education	Private Client	Transportation
Environmental	K12 Education	Public Entity	

Our specialized focus on these niche/practice groups allows for highly-focused marketing efforts and facilitates the development of value-added products and services specific to those industries. We believe that our detailed understanding and broad client contacts within these niche/practice groups provide us with a competitive advantage.

We anticipate that our retail brokerage operations greatest revenue growth over the next several years will continue to come from:

- Mergers and acquisitions;
- Our niche/practice groups and middle-market accounts;
- Cross-selling other brokerage products to existing clients; and
- Developing and managing alternative market mechanisms such as captives, rent-a-captives and deductible plans/self-insurance.

Wholesale Insurance Brokerage Operations

Our wholesale insurance brokerage operations accounted for 16% of our brokerage segment revenues in 2018. Our wholesale brokers assist our retail brokers and other non-affiliated brokers in the placement of specialized and hard-to-place insurance. These brokers operate through more than 295 offices primarily located across the U.S., Bermuda and through our approved Lloyd s of London brokerage operation. In certain cases we act as a brokerage wholesaler and in other cases we act as a managing general agent or managing general underwriter distributing specialized insurance coverages for underwriting enterprises. Managing general agents and managing general underwriters are agents authorized by an underwriting enterprise to manage all or a part of its business in a specific geographic territory. Activities they perform on behalf of the underwriting enterprise may include marketing, underwriting (although we do not assume any underwriting risk), issuing policies, collecting premiums, appointing and supervising other agents, paying claims and negotiating reinsurance.

More than 79% of our wholesale brokerage revenues comes from non-affiliated brokerage clients. Based on revenues, our domestic wholesale brokerage operation ranked as one of the largest domestic managing general agents/underwriting managers/wholesale brokers/Lloyds coverholders according to *Business Insurance* magazine s September 2018 edition.

We anticipate growing our wholesale brokerage operations by increasing the number of broker-clients, developing new managing general agency and underwriter programs, and through mergers and acquisitions.

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Risk Management Segment

Our risk management segment accounted for 14% of our revenues in 2018. Approximately 64% of our risk management segment s revenues are from workers compensation-related claims, 27% are from general and commercial auto liability-related claims and 9% are from property-related claims in 2018.

Risk management services are primarily marketed directly to Fortune 1000 companies, larger middle-market companies, not for profit organizations and public entities on an independent basis from our brokerage operations. We manage our third party claims adjusting operations through a network of more than 95 offices located throughout the U.S., Australia, Canada, New Zealand and the U.K. Most of these offices are fully staffed with claims adjusters and other service personnel. Our adjusters and service personnel act solely on behalf and under the instruction of our clients.

While this segment complements our brokerage and consulting offerings, more than 90% of our risk management segment s revenues come from clients not affiliated with our brokerage operations, such as underwriting enterprises and clients of other insurance brokers. Based on revenues, our risk management operation ranked as one of the world s largest property/casualty third party claims administrators according to *Business Insurance* magazine s May 2018 edition.

Revenues for our risk management segment are comprised of fees generally negotiated (i) on a per-claim basis, (ii) on a cost-plus basis, or (iii) as performance-based fees. We also provide risk management consulting services that are recognized as the services are delivered.

Per-claim fees

Where we operate under a contract with our fee established on a per-claim basis, our obligation is to process claims for a term specified within the contract. Because it is impractical to recognize our revenues on an individual claim-by-claim basis, we recognize revenue plus an appropriate estimate of our profit margin on a portfolio basis by grouping claims with similar characteristics (a practical expedient as defined in ASU No. 2014-09, Revenue from Contracts with Customers, which we refer to as Topic 606). We apply actuarially-determined, historical-based patterns to determine our future service obligations, without applying a present value discount.

Cost-plus fees

Where we provide services and generate revenues on a cost-plus basis, we recognize revenue over the contract period consistent with the performance of our obligations.

Performance-based fees

Certain clients pay us additional fee revenues for our efficiency in managing claims or on the basis of claim outcome effectiveness. These amounts are in excess of the fee revenues discussed above. These revenues are variable, generally based on various performance metrics of the underlying contracts. We generally operate under multi-year contracts with fiscal year measurement periods. We do not receive these fees, if earned, until the following year after verification of the performance metrics outlined in the contracts. Each period we base our estimates on a contract-by-contract basis. We make our best estimate of amounts we have earned using historical averages and other factors to project such revenues. Variable consideration is recognized when we conclude that is it probable that a significant revenue reversal will not occur in future periods.

We expect that the risk management segment s most significant growth prospects through the next several years will come from:

- Program business and the outsourcing of portions of underwriting enterprise claims departments;
- Increased levels of business with Fortune 1000 companies;
- Larger middle-market companies and captives; and

Mergers and acquisitions.

Corporate Segment

The corporate segment accounted for 25% of our revenues in 2018. The corporate segment reports the financial information related to our debt, clean energy investments, external acquisition-related expenses, other corporate costs and the impact of foreign currency translation. The revenues reported by this segment result almost solely from our consolidated clean energy investments.

Clean-Energy Investments

We own 34 commercial clean coal production facilities that produce refined coal using Chem-Mod LLC s proprietary technologies. These operations produce refined coal that we believe qualifies for tax credits under Internal Revenue Code (which we refer to as IRC) Section 45. The law that provides for IRC Section 45 tax credits will expire in December 2019 for 14 of our plants and in December 2021 for the other 20 plants. Chem-Mod LLC (described below) is a privately-held enterprise that has commercialized multi-pollutant reduction technologies to reduce mercury, sulfur dioxide and other emissions at coal-fired power plants. We own 46.5% of Chem-Mod LLC and are its controlling managing member. We also have a 12.0% noncontrolling interest in dormant, privately-held, enterprises, C-Quest Technology LLC and C-Quest Technologies International LLC (which we refer to as together, C-Quest), which owns technologies that reduce carbon dioxide emissions created by burning fossil fuels. At this time, it is unclear if C-Quest will ever become commercially viable.

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International and Other Brokerage Related Operations

We operate as a retail commercial property and casualty broker throughout more than 43 locations in Australia, 41 locations in Canada and 36 locations in New Zealand. In the U.K., we operate as a retail broker from approximately 105 locations. We also have specialty, wholesale, underwriting and reinsurance intermediary operations in London for clients to access Lloyd s of London and other international underwriting enterprises, and a program operation offering customized risk management products and services to U.K. public entities.

In Bermuda, we act principally as a wholesale broker for clients looking to access Bermuda-based underwriting enterprises and we also provide management and administrative services for captive insurance entities.

We also have strategic brokerage alliances with a variety of independent brokers in countries where we do not have a local office presence. Through this global network of correspondent insurance brokers and consultants, we are able to serve our clients coverage and service needs in more than 150 countries around the world.

Captive underwriting enterprises - We have ownership interests in several underwriting enterprises based in the U.S., Bermuda, Gibraltar, Guernsey, Isle of Man and Malta, that primarily operate segregated account rent-a-captive facilities. These rent-a-captive facilities enable our clients to receive the benefits of participating in a captive underwriting enterprise without incurring certain disadvantages of ownership. Captive underwriting enterprises, or rent-a-captive facilities, are created for clients to insure their risks and capture any underwriting profit and investment income, which would then be available for use by the insureds, generally to reduce future costs of their insurance programs. In general, these companies are set up as protected cell companies that are comprised of separate cell business units (which we refer to as Captive Cells) and the core regulated company (which we refer to as the Core Company). The Core Company is owned and operated by us and no insurance policies are assumed by the Core Company. All insurance is assumed or written within individual Captive Cells. Only the activity of the supporting Core Company of the rent-a-captive facility is recorded in our consolidated financial statements, including cash and stockholder s equity of the legal entity, and any expenses incurred to operate the rent-a-captive facility. Most Captive Cells reinsure individual lines of insurance coverage from external underwriting enterprises. In addition, some Captive Cells offer individual lines of insurance coverage from one of our underwriting enterprise subsidiaries. The different types of insurance coverage include special property, general liability, products liability, medical professional liability, other liability and medical stop loss. The policies are generally claims-made. Insurance policies are written by an underwriting enterprise and the risk is assumed by each of the Captive Cells. In general, we structure these operations to have no underwriting risk on a net written basis. In situations where we have assumed underwriting risk on a net written basis, we have managed that exposure by obtaining full collateral for the underwriting risk we have assumed from our clients. We typically require pledged assets including cash and/or investment accounts, or letters of credit to limit our risk.

We also have a wholly owned underwriting enterprise subsidiary based in the U.S. that cedes all of its insurance risk of loss to reinsurers or captives under facultative and quota-share treaty reinsurance agreements. While we believe these ceding reinsurance agreements displace all of our risk of loss, they do not discharge us of our primary liability to our clients. For example, in the event that all or any of the reinsuring companies or captives are unable to meet their obligations, we would be liable for such defaulted amounts. Therefore, we are subject to credit risk with respect to the obligations of our reinsurers or captives. In order to minimize our exposure to losses from reinsurer credit risk and insolvencies, we believe we have managed that exposure by obtaining full collateral, typically requiring pledged assets, including cash and/or investment accounts or letters of credit to offset the risk. See Note 17 to our 2018 consolidated financial statements for additional financial information related to the insurance activity of our wholly owned underwriting enterprise subsidiary for 2018, 2017 and 2016.

Competition

Brokerage Segment

According to *Business Insurance* magazine s July 2018 edition, we were the world s fourth largest insurance broker based on revenues. The insurance brokerage and consulting business is highly competitive and there are many organizations and individuals throughout the world who actively compete with us in every area of our business.

Our retail and wholesale brokerage operations compete globally with Aon plc, Marsh & McLennan Companies, Inc. and Willis Towers Watson Public Limited Company, each of which has greater worldwide revenues than us. In addition, various other competing firms, such as Brown & Brown Inc., Hub International Ltd., Lockton Companies, Inc., USI Holdings Corporation and BB&T Insurance Services operate globally or nationally or are strong in a particular region or locality and may have, in that region or locality, an office with revenues as large as or larger than those of our corresponding local office. Our wholesale brokerage and binding operations compete with large wholesalers such as CRC Insurance Services, Inc., RT Specialty, AmWINS Group, Inc., Burns & Wilcox, Ltd. and All Risks Ltd., as well as a vast number of local and regional wholesalers. We also compete with certain underwriting enterprises that offer insurance and risk management products and solutions directly to clients. In addition, for our employee benefit consulting services, we compete with larger firms such as Aon plc, Mercer (a subsidiary of Marsh & McLennan Companies, Inc.); Willis Towers Watson Public Limited Company; mid-market firms such as Lockton Companies, Inc. and USI Holdings Corporation, specialized consulting firms such as Pearl Meyer, and the benefits consulting divisions of the national public accounting firms, as well as a vast number of local and regional brokerages and agencies. Government benefits relating to health, disability and retirement are also alternatives to private insurance, and indirectly compete with us.

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We believe that the primary factors determining our competitive position with other organizations in our industry are the quality of the services we render, the personalized attention we provide, the individual and corporate expertise providing the actual service to the client, and the overall cost to our clients.

Risk Management Segment

Our risk management operation currently ranks as one of the world s largest property/casualty third party claims administrators based on revenues, according to *Business Insurance* magazine s May 2018 edition. While many global and regional claims administrators operate within this space, we compete directly with Sedgwick Claims Management Services, Inc., and Broadspire Services, Inc. (a subsidiary of Crawford & Company). Several large underwriting enterprises, such as Chubb Limited, Travelers Companies, Inc. and Liberty Mutual Holding Co, Inc. also maintain their own claims administration units, which can be strong competitors. In addition, we compete with various smaller third party claims administrators on a regional level. We believe that the primary factors determining our competitive position are our ability to deliver better claim outcomes, reputation for outstanding service, cost-efficient service and financial strength.

Business Combinations

We completed and integrated 507 acquisitions from January 1, 2002 through December 31, 2018, most of which were within our brokerage segment. The majority of these acquisitions have been smaller regional or local brokerages, agencies, or employee benefit consulting operations with a middle or small client focus and/or significant expertise in one of our niche/practice groups. The total purchase price for individual acquisitions has typically ranged from $1.0 million to $50.0 million.

Through acquisitions, we seek to expand our talent pool, enhance our geographic presence and service capabilities, and/or broaden and further diversify our business mix. We also focus on identifying:

- A corporate culture that matches our sales-oriented and ethics-based culture;
- A profitable, growing business whose ability to compete would be enhanced by gaining access to our greater resources; and
- Clearly defined financial criteria.

See Note 4 to our 2018 consolidated financial statements for a summary of our 2018 acquisitions, the amount and form of the consideration paid and the dates of acquisitions.

Clients

Our client base is highly diversified and includes commercial, industrial, public entity, religious and not-for-profit entities. No material part of our business depends upon a single client or on a few clients. The loss of any one client would not have a material adverse effect on our operations. In 2018, our largest single client represented approximately 1.0% and our ten largest clients together represented approximately 3.0% of our combined brokerage and risk management segment revenues.

Employees

As of December 31, 2018, we had approximately 30,400 employees.

We enter into agreements with many of our brokerage salespersons and significant client-facing employees, plus all of our executive officers, which prohibit them from disclosing confidential information and/or soliciting our clients, prospects and employees upon their termination of employment. The confidentiality and non-solicitation provisions of such agreements terminate in the event of a hostile change in control, as defined in the agreements. We pursue legal actions for alleged breaches of non-compete or other restrictive covenants, theft of trade secrets, breaches of fiduciary duties, intellectual property infringement and related causes of action.

Available Information

Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, are available free of charge on our website at http://investor.ajg.com/sec-filings as soon as reasonably practicable after electronically filing or furnishing such material to the Securities and Exchange Commission. The Securities and Exchange Commission also maintains a website (www.sec.gov) that includes our reports, proxy statements and other information.

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Item 1A. Risk Factors.

Risks Relating to our Business Generally

An economic downturn, as well as unstable economic conditions in the countries and regions in which we operate, could adversely affect our results of operations and financial condition.

A decline in economic activity could adversely impact us in future years as a result of reductions in the amount of insurance coverage and consulting services that our clients purchase due to reductions in their headcount, payroll, properties, and the market values of assets, among other factors. In addition, specific industries or sectors of the economy could experience declines in ways that impact our business; for example, if climate change and environmental risks harm the oil and gas industry, clients in our energy niche could go out of business or have reduced needs for insurance coverage or consulting services. All such reductions (whether caused by an overall economic decline or declines in particular industries) could adversely impact future commission revenues when the underwriting enterprises perform exposure audits if they lead to subsequent downward premium adjustments. We record the commission income effects of subsequent premium adjustments when the adjustments become known and, as a result, any downturn or improvement in our results of operations and financial condition may lag a downturn or improvement in the economy. Some of our clients may experience liquidity problems or other financial difficulties in the event of a prolonged deterioration in the economy, which could have an adverse effect on our results of operations and financial condition. If our clients become financially less stable, enter bankruptcy, liquidate their operations or consolidate, our revenues and collectability of receivables could be adversely affected.

The exit of the U.K. from the European Union (Brexit) could adversely affect our results of operations and financial condition.

Our operations in the U.K., which contributed approximately 17% of our brokerage segment and approximately 4% of our risk management segment revenues in 2018, expose us to risk in the event of an economic downturn in the U.K. due to Brexit. Such a downturn could adversely affect our U.K. operations through a decline in the insurance coverage and consulting services our clients purchase as they face reductions in their headcount, payroll, properties or the market value of their assets. In a so-called hard or no-deal Brexit where the U.K. leaves the European Union without trade or other deals in place with member countries, our European client base outside the U.K., which is minimal, would need to be serviced from operations in a country in the European Union. While we have a plan in place to service these clients from one of our existing offices in Sweden, such a transition could be a distraction to both clients and our management. In addition, the uncertainty surrounding Brexit has and may continue to result in substantial volatility in foreign exchange markets and may lead to a sustained weakness in the British pound s exchange rate against the U.S. dollar. Any significant weakening of the British pound to the U.S. dollar will have an adverse impact on our brokerage and risk management segments net earnings as reported in U.S. dollars.

Economic conditions that result in financial difficulties for underwriting enterprises or lead to reduced risk-taking capital capacity could adversely affect our results of operations and financial condition.

We have a significant amount of trade accounts receivable from some of the underwriting enterprises with which we place insurance. If those companies experience liquidity problems or other financial difficulties, we could encounter delays or defaults in payments owed to us, which could have a significant adverse impact on our consolidated financial condition and results of operations. The failure of an underwriting enterprise with which we place business could result in errors and omissions claims against us by our clients, and the failure of errors and omissions underwriting enterprises could make the errors and omissions insurance we rely upon cost prohibitive or unavailable, which could adversely affect our results of operations and financial condition. In addition, if underwriting enterprises merge or if a large underwriting enterprise fails or withdraws from offering certain lines of coverage, overall risk-taking capital capacity could be negatively affected, which could reduce our ability to place certain lines of coverage and, as a result, reduce our revenues and profitability. Such failures or coverage withdrawals on the part of underwriting enterprises could occur for any number of reasons, including large unexpected payouts related to climate change or other emerging risk areas.

We have historically acquired large numbers of insurance brokers, benefit consulting firms and, to a lesser extent, claim and risk management firms. We may not be able to continue such an acquisition strategy in the future and there are risks associated with such acquisitions, which could adversely affect our growth and results of operations.

Our acquisition program has been an important part of our historical growth, particularly in our brokerage segment, and we believe that similar acquisition activity will be important to maintaining comparable growth in the future. Failure to successfully identify and complete acquisitions likely would result in us achieving slower growth. Continuing consolidation in our industry and growing interest in acquiring insurance brokers on the part of private equity firms and private equity-backed consolidators could make it more difficult for us to identify appropriate targets and could make them more expensive. Even if we are able to identify appropriate acquisition targets, we may not have sufficient capital to fund acquisitions, be able to execute transactions on favorable terms or integrate targets in a manner that allows us to realize the benefits we have historically experienced from acquisitions. When regulatory approval of acquisitions is required, our ability to complete acquisitions may be limited by an ongoing regulatory review or other issues with the relevant regulator. Our ability to finance and integrate acquisitions may also decrease if we complete a greater number of large acquisitions than we have historically.

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Post-acquisition risks include those relating to retention of personnel, retention of clients, entry into unfamiliar markets or lines of business, contingencies or liabilities, such as violations of sanctions laws or anti-corruption laws including the FCPA and U.K. Bribery Act, risks relating to ensuring compliance with licensing and regulatory requirements, tax and accounting issues, the risk that the acquisition distracts management and personnel from our existing business, and integration difficulties relating to accounting, information technology, human resources, employee attrition or poor organizational culture and fit, some or all of which could have an adverse effect on our results of operations and growth. The failure of acquisition targets to achieve anticipated revenue and earnings levels could also result in goodwill impairment charges.

We own interests in firms where we do not exercise management control (such as Casanueva Perez S.A.P. de C.V. in Mexico) and are therefore unable to direct or manage the business to realize the anticipated benefits, including mitigation of risks, that could be achieved through full integration.

We face significant competitive pressures in each of our businesses.

The insurance brokerage and employee benefit consulting businesses are highly competitive and many insurance brokerage and employee benefit consulting organizations actively compete with us in one or more areas of our business around the world. We compete with three firms in the global risk management and brokerage markets that have revenues significantly larger than ours. In addition, many other smaller firms that operate nationally or that are strong in a particular country, region or locality may have, in that country, region or locality, an office with revenues as large as or larger than those of our corresponding local office. Our third party claims administration operation also faces significant competition from stand-alone firms as well as divisions of larger firms.

We believe that the primary factors determining our competitive position with other organizations in our industry are the quality of the services we render, the personalized attention we provide, the individual and corporate expertise of the brokers and consultants providing the actual service to the client and our ability to help our clients manage their overall insurance costs. Losing business to competitors offering similar products at a lower cost or having other competitive advantages would adversely affect our business.

In addition, any increase in competition due to new legislative or industry developments could adversely affect us. These developments include:

- Increased capital-raising by underwriting enterprises, which could result in new risk-taking capital in the industry, which in turn may lead to lower insurance premiums and commissions;
- Underwriting enterprises selling insurance directly to insureds without the involvement of a broker or other intermediary;
- Changes in our business compensation model as a result of regulatory developments;
- Federal and state governments establishing programs to provide health insurance or, in certain cases, property insurance in catastrophe-prone areas or other alternative market types of coverage, that compete with, or completely replace, insurance products currently offered by underwriting enterprises; and
- Increased competition from new market participants such as banks, accounting firms, consulting firms and Internet or other technology firms offering risk management or insurance brokerage services, or new distribution channels for insurance such as payroll firms.

New competition as a result of these or other legislative or industry developments could cause the demand for our products and services to decrease, which could in turn adversely affect our results of operations and financial condition.

Volatility or declines in premiums or other adverse trends in the insurance industry may seriously undermine our profitability.

We derive much of our revenue from commissions and fees for our brokerage services. We do not determine the insurance premiums on which our commissions are generally based. Moreover, insurance premiums are cyclical in nature and may vary widely based on market conditions. Because of market cycles for insurance product pricing, which we cannot predict or control, our brokerage revenues and profitability can be volatile or remain depressed for significant periods of time.

As underwriting enterprises continue to outsource the production of premium revenue to non-affiliated brokers or agents such as us, those companies may seek to further minimize their expenses by reducing the commission rates payable to insurance agents or brokers. The reduction of these commission rates, along with general volatility and/or declines in premiums, may significantly affect our profitability. Because we do not determine the timing or extent of premium pricing changes, it is difficult to precisely forecast our commission revenues, including whether they will significantly decline. As a result, we may have to adjust our budgets for future acquisitions, capital expenditures, dividend payments, loan repayments and other expenditures to account for unexpected changes in revenues, and any decreases in premium rates may adversely affect the results of our operations.

In addition, there have been and may continue to be various trends in the insurance industry toward alternative insurance markets including, among other things, greater levels of self-insurance, captives, rent-a-captives, risk retention groups and non-insurance capital markets-based solutions to traditional insurance. While historically we have been able to participate in certain of these activities on behalf of our clients and obtain fee revenue for such services, there can be no assurance that we will realize revenues and profitability as favorable as those realized from our traditional brokerage activities. Our ability to generate premium-based commission revenue may also be challenged by the growing desire of some clients to compensate brokers based upon flat fees rather than variable commission rates. This could negatively impact us because fees are generally not indexed for inflation and do not automatically increase with premiums as commissions do.

Contingent and supplemental revenues we receive from underwriting enterprises are less predictable than standard commission revenues, and any decrease in the amount of these forms of revenue could adversely affect our results of operations.

A significant portion of our revenues consists of contingent and supplemental revenues from underwriting enterprises. Contingent revenues are paid after the insurance contract period, generally in the first or second quarter, based on the growth and/or profitability of business we placed with an underwriting enterprise during the prior year. On the other hand, supplemental revenues are paid up front, on an annual or quarterly basis, generally based on our historical premium volumes with the underwriting enterprise and additional capabilities or services we bring to the engagement. If, due to the current economic environment or for any other reason, we are unable to meet an underwriting enterprise s particular profitability, volume or growth thresholds, as the case may be, or such companies increase their estimate of loss reserves (over which we have no control), actual contingent revenues or supplemental revenues could be less than anticipated, which could adversely affect our results of operations. In the case of contingent revenues, under the new revenue recognition accounting standard, that was effective January 1, 2018, this could lead to the reversal of revenues in future periods that were recognized in prior periods (See Note 2 to our 2018 consolidated financial statements for more information).

If we are unable to apply technology effectively in driving value for our clients through technology-based solutions or gain internal efficiencies and effective internal controls through the application of technology and related tools, our operating results, client relationships, growth and compliance programs could be adversely affected.

Our future success depends, in part, on our ability to anticipate and respond effectively to the threat and opportunity presented by digital disruption and developments in technology. These may include new applications or insurance-related services based on artificial intelligence, machine learning, robotics, blockchain or new approaches to data mining. We may be exposed to competitive risks related to the adoption and application of new technologies by established market participants (for example, through disintermediation) or new entrants such as technology companies, Insurtech start-up companies and others. These new entrants are focused on using technology and innovation, including artificial intelligence and blockchain, to simplify and improve the client experience, increase efficiencies, alter business models and effect other potentially disruptive changes in the industries in which we operate. We must also develop and implement technology solutions and technical expertise among our employees that anticipate and keep pace with rapid and continuing changes in technology, industry standards, client preferences and internal control standards. We may not be successful in anticipating or responding to these developments on a timely and cost-effective basis and our ideas may not be accepted in the marketplace. Additionally, the effort to gain technological expertise and develop new technologies in our business requires us to incur significant expenses. If we cannot offer new technologies as quickly as our competitors, or if our competitors develop more cost-effective technologies or product offerings, we could experience a material adverse effect on our operating results, client relationships, growth and compliance programs.

In some cases, we depend on key third-party vendors and partners to provide technology and other support for our strategic initiatives. If these third parties fail to perform their obligations or cease to work with us, our ability to execute on our strategic initiatives could be adversely affected.

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Damage to our reputation could have a material adverse effect on our business.

Our reputation is one of our key assets. We advise our clients on and provide services related to a wide range of subjects and our ability to attract and retain clients is highly dependent upon the external perceptions of our level of service, ability to protect client information, trustworthiness, business practices, financial condition and other subjective qualities such as culture and values. Our success is also dependent on maintaining a good reputation with existing and potential employees, investors and regulators. Negative perceptions or publicity regarding the matters noted above, including our association with clients or business partners who themselves have a damaged reputation, or from actual or alleged conduct by us or our employees, could damage our reputation. Our reputation could also be impacted by negative perceptions or publicity regarding environmental, social and governance (ESG) issues or cybersecurity and data privacy concerns. Any resulting erosion of trust and confidence could make it difficult for us to attract and retain clients, employees and investors or harm our relationships with regulators, any of which could have a material adverse effect on our business, financial condition and results of operations.

Our future success depends, in part, on our ability to attract and retain experienced and qualified talent, including our senior management team.

We depend upon members of our senior management team, who possess extensive knowledge and a deep understanding of our business and strategy. We could be adversely affected if we fail to plan adequately for the succession of these leaders, including our chief executive officer. We could also be adversely affected if we fail to attract and retain talent throughout our organization. Competition for talent in rapidly developing fields such as artificial intelligence and data engineering is particularly intense. In addition, our industry has experienced competition for leading brokers and in the past we have lost key brokers and groups of brokers, along with their clients, business relationships and intellectual property directly to our competition. Our failure to adequately address any of these issues could have a material adverse effect on our business, operating results and financial condition.

Our substantial operations outside the U.S. expose us to risks different than those we face in the U.S.

In 2018, we generated approximately 30% of our combined brokerage and risk management revenues outside the U.S. The global nature of our business creates operational and economic risks. Adverse geopolitical or economic conditions may temporarily or permanently disrupt our operations outside the U.S. or create difficulties in staffing and managing such operations. For example, we have substantial operations in India that provide important back-office services for other parts of our global organization. To date, the dispute between India and Pakistan involving the Kashmir region, incidents of terrorism in India and general geopolitical uncertainties have not adversely affected our operations in India. However, such factors could potentially affect our operations there in the future. Should our access to these services be disrupted, our business, operating results and financial condition could be adversely affected.

Operating outside the U.S. may also present other risks that are different from, or greater than, the risks we face doing comparable business in the U.S. These include, among others, risks relating to:

- Maintaining awareness of and complying with a wide variety of labor practices and foreign laws, including those relating to export and import duties, environmental policies and privacy issues, as well as laws and regulations applicable to U.S. business operations abroad. These and other international regulatory risks are described below under Regulatory, Legal and Accounting Risks;

- The potential costs, difficulties and risks associated with local regulations across the globe, including the risk of personal liability for directors and officers and piercing the corporate veil risks under the corporate law regimes of certain countries;

- Difficulties in staffing and managing foreign operations. For example, we are building our South American operations (which contributed $32.3 million in revenue from 15 locations in 2018) through acquisitions of local family-owned insurance brokerage firms. If we lose a local leader, recruiting a replacement locally or finding an internal candidate qualified to transfer to such location could be difficult;

- Less flexible employee relationships, which may limit our ability to prohibit employees from competing with us after they are no longer employed with us or recovering damages in the event they do so, and may make it more difficult and expensive to terminate their employment;

Some of our foreign subsidiaries receive revenues or incur obligations in currencies that differ from their functional currencies. We must also translate the financial results of our foreign subsidiaries into U.S. dollars. Although we have used foreign currency hedging strategies in the past and currently have some in place, such risks cannot be eliminated entirely, and significant changes in exchange rates may adversely affect our results of operations;

Conflicting regulations in the countries in which we do business;

Political and economic instability (including risks relating to undeveloped or evolving legal systems, unstable governments, acts of terrorism and outbreaks of war);

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- Coordinating our communications and logistics across geographic distances, multiple time zones and in different languages, including during times of crisis management;

- Adverse trade policies, and adverse changes to any of the policies of the U.S. or any of the foreign jurisdictions in which we operate;

- The transition away from LIBOR to the Secured Overnight Financing Rate as a benchmark reference for short-term interest rates;

- Unfavorable audits and exposure to additional liabilities relating to various non-income taxes (such as payroll, sales, use, value-added, net worth, property and goods and services taxes) in foreign jurisdictions. In addition, our future effective tax rates could be unfavorably affected by changes in tax rates, discriminatory or confiscatory taxation, changes in the valuation of our deferred tax assets or liabilities, changes in tax laws or their interpretation and the financial results of our international subsidiaries. The Organization for Economic Cooperation and Development issued reports and recommendations as part of its Base Erosion and Profit Shifting project (which we refer to as BEPS), and in response many countries in which we do business are expected to adopt rules which may change various aspects of the existing framework under which our tax obligations are determined. For example, in response to BEPS, the U.K., Australia and New Zealand adopted rules that affect the deductibility of interest paid on intercompany debt, and other jurisdictions where we operate may do so as well in the near future;

- Legal or political constraints on our ability to maintain or increase prices;

- Cash balances held in foreign banks and institutions where governments have not specifically enacted formal guarantee programs;

- Lost business or other financial harm due to governmental actions affecting the flow of goods, services and currency, including protectionist policies that discriminate in favor of local competitors; and

- Governmental restrictions on the transfer of funds to us from our operations outside the U.S.

The trade policies of the current U.S. presidential administration could develop in ways that exacerbate the risks described above, or introduce new risks for our international operations. If any of these risks materialize, our results of operations and financial condition could be adversely affected.

We face a variety of risks in our risk management third-party claims administration operations that are distinct from those we face in our insurance brokerage and benefit consulting operations.

Our third party claims administration operations face a variety of risks distinct from those faced by our brokerage operations, including the risks that:

- The favorable trend among both underwriting enterprises and self-insured entities toward outsourcing various types of claims administration and risk management services will reverse or slow, causing our revenues or revenue growth to decline;

- Concentration of large amounts of revenue with certain clients results in greater exposure to the potential negative effects of lost business due to changes in management at such clients or changes in state government policies, in the case of our government-entity clients, or for other reasons;

Contracting terms will become less favorable or the margins on our services will decrease due to increased competition, regulatory constraints or other developments;

We will not be able to satisfy regulatory requirements related to third party administrators or regulatory developments (including those relating to security and data privacy outside the U.S.) will impose additional burdens, costs or business restrictions that make our business less profitable;

Our revenue is impacted by case volumes, which are dependent upon a number of factors and difficult to forecast accurately;

Economic weakness or a slow-down in economic activity could lead to a reduction in the number of claims we process;

If we do not control our labor and technology costs, we may be unable to remain competitive in the marketplace and profitably fulfill our existing contracts (other than those that provide cost-plus or other margin protection);

We may be unable to develop further efficiencies in our claims-handling business and may be unable to obtain or retain certain clients if we fail to make adequate improvements in technology or operations; and

Underwriting enterprises or certain large self-insured entities may create in-house servicing capabilities that compete with our third party administration and other administration, servicing and risk management products.

If any of these risks materialize, our results of operations and financial condition could be adversely affected.

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Sustained increases in the cost of employee benefits could reduce our profitability.

The cost of current employees medical and other benefits, as well as pension retirement benefits and postretirement medical benefits under our legacy defined benefit plans, substantially affects our profitability. In the past, we have occasionally experienced significant increases in these costs as a result of macro-economic factors beyond our control, including increases in health care costs, declines in investment returns on pension assets and changes in discount rates and actuarial assumptions used to calculate pension and related liabilities. A significant decrease in the value of our defined benefit pension plan assets, changes to actuarial assumptions used to determine pension plan liabilities, or decreases in the interest rates used to discount the pension plans liabilities could cause an increase in pension plan costs in future years. Although we have actively sought to control increases in these costs, we can make no assurance that we will succeed in limiting future cost increases, and continued upward pressure in these costs could reduce our profitability.

Business disruptions could have a material adverse effect on our operations, damage our reputation and impact client relationships.

Our ability to conduct business may be adversely affected by a disruption in the infrastructure that supports our business. Such a disruption could be caused by human error, capacity constraints, hardware failure or defect, natural disasters, fire, power loss, telecommunication failures, break-ins, sabotage, intentional acts of vandalism, acts of terrorism, political unrest, or war. Our disaster recovery procedures may not be effective and insurance may not continue to be available at reasonable prices and may not address all such losses or compensate us for the possible loss of clients or increase in claims and lawsuits directed against us.

For example, our third party claims administration operation is highly dependent on the continued and efficient functioning of RISX-FACS®, our proprietary risk management information system, to provide clients with insurance claim settlement and administration services. A disruption affecting RISX-FACS® or any other infrastructure supporting our business could have a material adverse effect on our operations, cause reputational harm and damage our client relationships.

Regulatory, Legal and Accounting Risks

A cybersecurity attack could adversely affect our business, financial condition and reputation.

We rely on information technology and third party vendors to support our business activities, including our secure processing of confidential sensitive, proprietary and other types of information. Cybersecurity breaches of any of the systems we rely on may result from circumvention of security systems, denial-of-service attacks or other cyber-attacks, hacking, phishing attacks, computer viruses, ransomware, malware, employee or insider error, malfeasance, social engineering, physical breaches or other actions. We have from time to time experienced cybersecurity breaches, such as computer viruses, unauthorized parties gaining access to our information technology systems and similar incidents, which to date have not had a material impact on our business. Additionally, we are an acquisitive organization and the process of integrating the information systems of the businesses we acquire is complex and exposes us to additional risk as we might not adequately identify weaknesses in the targets information systems, which could expose us to unexpected liabilities or make our own systems more vulnerable to attack. In the future, any material breaches of cybersecurity, or media reports of the same, even if untrue, could cause us to experience reputational harm, loss of clients and revenue, loss of proprietary data, regulatory actions and scrutiny, sanctions or other statutory penalties, litigation, liability for failure to safeguard clients information or financial losses. Such losses may not be insured against or not fully covered through insurance we maintain.

We have invested and continue to invest in technology security initiatives, policies and resources and employee training. The cost and operational consequences of implementing, maintaining and enhancing further system protections measures could increase significantly as cybersecurity threats increase. As these threats evolve, cybersecurity incidents will be more difficult to detect, defend against and remediate. Any of the foregoing may have a material adverse effect on our business, financial condition and reputation.

Improper disclosure of confidential, personal or proprietary information could result in regulatory scrutiny, legal liability or reputational harm, and could have an adverse effect on our business or operations.

We maintain confidential, personal and proprietary information relating to our company, our employees and our clients. This information includes personally identifiable information, protected health information, financial information and intellectual property. If our information systems or infrastructure or those of our third party vendors experience a significant disruption or breach, such information could be compromised. A party that obtains this information may use it to steal funds, for ransom, to facilitate a fraud, or for other illicit purposes. Such a disruption or breach could also result in unauthorized access to our proprietary information, intellectual property and business secrets.

We maintain policies, procedures and technical safeguards designed to protect the security and privacy of confidential, personal and proprietary information. Nonetheless, we cannot eliminate the risk of human error or malfeasance. It is possible that our security controls and employee training may not be effective. This could harm our reputation, create legal exposure, or subject us to legal liability. Significant costs are involved with maintaining system safeguards for our technology infrastructure. If we are unable to effectively maintain and upgrade our system safeguards, including in connection with the integration of acquisitions, we may incur unexpected costs and certain of our systems may become more vulnerable to unauthorized access.

With respect to our commercial arrangements with third party vendors, we have processes designed to require third party IT outsourcing, offsite storage and other vendors to agree to maintain certain standards with respect to the storage, protection and transfer of confidential, personal and proprietary information. However, we remain at risk of a data breach due to the intentional or unintentional non-compliance by a vendor s employee or agent, the breakdown of a vendor s data protection processes, or a cyber attack on a vendor s information systems.

Changes in data privacy and protection laws and regulations, or any failure to comply with such laws and regulations, could adversely affect our business and financial results.

We are subject to a variety of continuously evolving and developing laws and regulations globally regarding privacy, data protection, and data security, including those related to the collection, storage, handling, use, disclosure, transfer, and security of personal data. Significant uncertainty exists as privacy and data protection laws may be interpreted and applied differently from country to country and may create inconsistent or conflicting requirements. These laws apply to transfers of information among our affiliates, as well as to transactions we enter into with third party vendors. For example, the European Union adopted a comprehensive General Data Privacy Regulation (GDPR) in May 2016 that replaced the former EU Data Protection Directive and related country-specific legislation. The GDPR became fully effective in May 2018, and requires companies to satisfy new requirements regarding the handling of personal and sensitive data, including its use, protection and the ability of persons whose data is stored to correct or delete such data about themselves. Failure to comply with GDPR requirements could result in penalties of up to 4% of worldwide revenue. Complying with the enhanced obligations imposed by the GDPR may result in significant costs to our business and require us to revise certain of our business practices. In addition, legislators and regulators in the U.S. have enacted and are proposing new and more robust privacy and cybersecurity laws and regulations in light of the recent broad-based cyber attacks at a number of companies, including but not limited to the New York State Department of Financial Services Cybersecurity Requirements for Financial Services Companies and the California Consumer Privacy Act of 2018.

These and similar initiatives around the world could increase the cost of developing, implementing or securing our servers and require us to allocate more resources to improved technologies, adding to our IT and compliance costs. In addition, enforcement actions and investigations by regulatory authorities related to data security incidents and privacy violations continue to increase. The enactment of more restrictive laws, rules, regulations, or future enforcement actions or investigations could impact us through increased costs or restrictions on our business, and noncompliance could result in regulatory penalties and significant legal liability.

We are subject to regulation worldwide. If we fail to comply with regulatory requirements or if regulations change in a way that adversely affects our operations, we may not be able to conduct our business, or we may be less profitable.

Many of our activities throughout the world are subject to regulatory supervision and regulations promulgated by bodies such as the Securities and Exchange Commission (which we refer to as SEC), the Department of Justice (which we refer to as DOJ), the IRS and the Office of Foreign Assets Control (which we refer to as OFAC) in the U.S., the Financial Conduct Authority (which we refer to as FCA) in the U.K., the Australian Securities and Investments Commission in Australia and insurance regulators in nearly every jurisdiction in which we operate. Our activities are also subject to a variety of other laws, rules and regulations addressing licensing, data privacy, wage-and-hour standards, employment and labor relations, anti-competition, anti-corruption, currency, reserves and the amount of local investment with respect to our operations in certain countries. This regulatory supervision could reduce our profitability or growth by increasing the costs of compliance, restricting the products or services we sell, the markets we enter, the methods by which we sell our products and services, or the prices we can charge for our services and the form of compensation we can accept from our clients, underwriting enterprises and third parties. As our operations grow around the world, it is increasingly difficult to monitor and enforce regulatory compliance across the organization. A compliance failure by even one of our smallest branches could lead to litigation and/or disciplinary actions that may include compensating clients for loss, the imposition of penalties and the revocation of our authorization to operate. In all such cases, we would also likely incur significant internal investigation costs and legal fees.

The global nature of our operations increases the complexity and cost of compliance with laws and regulations, including increased staffing needs, the development of new policies, procedures and internal controls and providing training to employees in multiple locations, adding to our cost of doing business. Many of these laws and regulations may have differing or conflicting legal standards across jurisdictions, increasing further the complexity and cost of compliance. In emerging markets and other jurisdictions with less developed legal systems, local laws and regulations may not be established with sufficiently clear and reliable guidance to provide us with adequate assurance that we are aware of all necessary licenses to operate our business, that we are operating our business in a compliant manner, or that our rights are otherwise protected. In addition, major political and legal developments in jurisdictions in which we do business may lead to new regulatory costs and challenges. See The exit of the U.K. from the European Union (Brexit) could adversely affect our results of operations and financial condition.

Changes in legislation or regulations and actions by regulators, including changes in administration and enforcement policies, could from time to time require operational changes that could result in lost revenues or higher costs or hinder our ability to operate our business.

For example, the method by which insurance brokers are compensated has received substantial scrutiny in the past because of the potential for conflicts of interest. The potential for conflicts of interest arises when a broker is compensated by two parties in connection with the same or similar transactions. The vast majority of the compensation we receive for our work as insurance brokers is in the form of retail commissions and fees. We receive additional revenue from underwriting enterprises, separate from retail commissions and fees, including, among other things, contingent and supplemental revenues and payments for consulting and analytics services we provide them. Future changes in the regulatory environment may impact our ability to collect these amounts. Adverse regulatory, legal or other developments regarding these revenues could have a material adverse effect on our business, results of operations or financial condition, expose us to negative publicity and reputational damage and harm our relationships with clients, underwriting enterprises or other business partners.

In addition, we have made significant investments in product and knowledge development to assist clients as they navigate the complex regulatory requirements relating to employer sponsored healthcare. Depending on future changes to health legislation, these investments may not yield returns. If we are unable to adapt our services to future changes in the legal and regulatory landscape around employer sponsored healthcare, our ability to grow our business or provide effective services, particularly in our employee benefits consulting business, will be negatively impacted. If our clients reduce the role or extent of employer sponsored healthcare in response to any future law or regulation, our results of operations could be adversely impacted.

We could be adversely affected by violations or alleged violations of laws that impose requirements for the conduct of our overseas operations, including the FCPA, the U.K. Bribery Act or other anti-corruption laws, sanctioned parties restrictions, and FATCA.

In foreign countries where we operate, a risk exists that our employees, third party partners or agents could engage in business practices prohibited by applicable laws and regulations, such as the FCPA and the U.K. Bribery Act. Such anti-corruption laws generally prohibit companies from making improper payments to foreign officials and require companies to keep accurate books and records and maintain appropriate internal controls. Our policies mandate strict compliance with such laws and we devote substantial resources to programs to ensure compliance. However, we operate in some parts of the world that have experienced governmental corruption, and, in certain circumstances, local customs and practice might not be consistent with the requirements of anti-corruption laws. In addition, in recent years, two of the five publicly traded insurance brokerage firms were investigated in the U.S. and the U.K. for improper payments to foreign officials. These firms undertook internal investigations and paid significant settlements.

We remain subject to the risk that our employees, third party partners or agents will engage in business practices that are prohibited by our policies and violate such laws and regulations. Violations by us or a third party acting on our behalf could result in significant internal investigation costs and legal fees, civil and criminal penalties, including prohibitions on the conduct of our business, and reputational harm.

We may also be subject to legal liability and reputational damage if we violate U.S. trade sanctions administered by OFAC, the European Union and the United Nations, and trade sanction laws such as the Iran Threat Reduction and Syria Human Rights Act of 2012.

In addition, FATCA requires certain of our subsidiaries, affiliates and other entities to obtain valid FATCA documentation from payees prior to remitting certain payments to such payees. In the event we do not obtain valid FATCA documents, we may be obliged to withhold a portion of such payments. This obligation is shared with our clients who may fail to comply, in whole or in part. In such circumstances, we may incur FATCA compliance costs including withholding taxes, interest and penalties. Recent regulatory developments related to FATCA could also cause short-term increases in our costs related to systems and process updates needed for us to be able to take advantage of such changes. In addition, the impact of Brexit on FATCA reporting for EU placements may further increase our compliance burden and cost of operations and could adversely affect the market for our services as intermediaries, which could adversely affect our results of operations and financial condition.

The Tax Cuts and Jobs Act may have an adverse effect on us, and such effect may be material.

On December 22, 2017, the U.S. enacted tax legislation commonly referred to as the Tax Cuts and Jobs Act (the Tax Act), which significantly revised the U.S. tax code by, among other things, lowering the corporate income tax rate from 35.0% to 21.0%; limiting the deductibility of interest expense; implementing a territorial tax system and imposing a repatriation tax on deemed repatriated earnings of foreign subsidiaries. Some aspects of the Tax Act are still unclear and will continue to be clarified over time. While we have updated estimates of the tax impacts based on guidance released to date or interpretations under such guidance, other guidance could be issued in the future, which could adversely affect our results of operations and financial condition.

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We are subject to a number of contingencies and legal proceedings which, if determined unfavorably to us, would adversely affect our financial results.

We are subject to numerous claims, tax assessments, lawsuits and proceedings that arise in the ordinary course of business. Such claims, lawsuits and other proceedings could, for example, include claims for damages based on allegations that our employees or sub-agents improperly failed to procure coverage, report claims on behalf of clients, provide underwriting enterprises with complete and accurate information relating to the risks being insured, or provide clients with appropriate consulting, advisory and claims handling services. There is the risk that our employees or sub-agents may fail to appropriately apply funds that we hold for our clients on a fiduciary basis. Certain of our benefits and retirement consultants provide investment advice or decision-making services to clients. If these clients experience investment losses, our reputation could be damaged and our financial results could be negatively affected as a result of claims asserted against us and lost business. We have established provisions against these matters that we believe are adequate in light of current information and legal advice, and we adjust such provisions from time to time based on current material developments. The damages claimed in such matters are or may be substantial, including, in many instances, claims for punitive, treble or other extraordinary damages. It is possible that, if the outcomes of these contingencies and legal proceedings were not favorable to us, it could materially adversely affect our future financial results. In addition, our results of operations, financial condition or liquidity may be adversely affected if, in the future, our insurance coverage proves to be inadequate or unavailable or we experience an increase in liabilities for which we self-insure. We have purchased errors and omissions insurance and other insurance to provide protection against losses that arise in such matters. Accruals for these items, net of insurance receivables, when applicable, have been provided to the extent that losses are deemed probable and are reasonably estimable. These accruals and receivables are adjusted from time to time as current developments warrant.

As more fully described in Note 16 to our 2018 consolidated financial statements, we are a defendant in various legal actions incidental to our business, including but not limited to matters related to employment practices, alleged breaches of non-compete or other restrictive covenants, theft of trade secrets, breaches of fiduciary duties, intellectual property infringement and related causes of action. We are also periodically the subject of inquiries and investigations by regulatory and taxing authorities into various matters related to our business. For example, our micro-captive advisory services are currently the subject of an investigation by the IRS and clients of that business brought a lawsuit against us alleging that the tax benefits associated with their micro-captives were disallowed by the IRS. In addition, Chem-Mod LLC is defending lawsuits asserting that various entities associated with our clean energy investments are liable for infringement of a patent held by Nalco Company. We cannot reasonably predict the outcomes of these or other matters that we may become involved with in the future. An adverse outcome in connection with one or more of these matters could have a material adverse effect on our business, results of operations or financial condition in any given quarterly or annual period, or on an ongoing basis. In addition, regardless of any eventual monetary costs, any such matter could expose us to negative publicity, reputational damage, harm to our client or employee relationships, or diversion of personnel and management resources, which could adversely affect our ability to recruit quality brokers and other significant employees to our business, and otherwise adversely affect our results of operations.

Changes in our accounting estimates and assumptions could negatively affect our financial position and operating results.

We prepare our financial statements in accordance with U.S. generally accepted accounting principles (which we refer to as GAAP). These accounting principles require us to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of our consolidated financial statements. We are also required to make certain judgments and estimates that affect the disclosed and recorded amounts of revenues and expenses related to the impact of the adoption of and accounting under Topic 606. We periodically evaluate our estimates and assumptions, including those relating to the valuation of goodwill and other intangible assets, investments (including our IRC Section 45 investments), income taxes, revenue recognition, deferred costs, stock-based compensation, claims handling obligations, retirement plans, litigation and contingencies. We base our estimates on historical experience and various assumptions that we believe to be reasonable based on specific circumstances. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed in our consolidated financial statements. Further, as additional guidance relating to the Tax Act is released, our estimates related to the Tax Act may change. Additionally, changes in accounting standards (such as the new revenue recognition standard and a new standard for leases - see Note 2 to our 2018 consolidated financial statements) could increase costs to the organization and could have an adverse impact on our future financial position and results of operations.

Risks Relating to our Investments, Debt and Common Stock

Our clean energy investments are subject to various risks and uncertainties.

Our ability to generate returns and avoid write-offs in connection with our IRC Section 45 and IRC Section 29 investments is subject to various risks and uncertainties including those set forth below.

Environmental concerns regarding coal. Environmental concerns about greenhouse gases, toxic wastewater discharges and the potential hazardous nature of coal combustion waste could lead to public pressure to reduce or regulations that discourage the burning of coal, even refined coal treated by technologies such as The Chem-

Mod Solution. Negative publicity regarding our IRC Section 45 investments or clean coal generally could exacerbate this risk and increase the risk that Congress might limit the availability of the tax credits or fail to extend them. Additionally, regulations could mandate that electric power generating companies purchase a minimum amount of power from energy sources such as wind, hydroelectric, solar, nuclear and geothermal. If utilities burned less coal as a result of any such regulation, our ability to generate tax credits would be reduced.

Demand for commercial refined coal plants. Changes in circumstances may cause a commercial refined coal plant to be moved to a different power generation facility, which could require us to invest additional capital. The implementation of environmental regulations regarding certain pollution control and permitting requirements has been delayed from time to time due to various lawsuits and changes in presidential administrations. The uncertainty created by litigation and reconsiderations of rule-making by the Environmental Protection Agency could negatively impact power generational facilities demand for commercial refined coal plants, should we need to move them. Sustained low natural gas prices could cause utilities to phase out or close existing coal-fired power plants. In addition, certain financing sources and insurance companies have taken action to limit available financing and insurance coverage for the development of new coal-fueled power plants, which could also limit the demand for refined coal facilities at power plants should we need to move one of our existing facilities.

Market demand for coal. When the price of natural gas and/or oil declines relative to that of coal, some utilities may choose to burn natural gas or oil instead of coal. Market demand for coal may also decline as a result of an increase in the use of wind generated power, an economic slowdown or mild weather and a corresponding decline in the use of electricity. If utilities burn less coal or eliminate coal in the production of electricity, the availability of the tax credits would also be reduced.

Intellectual property and litigation risks. There is a risk that foreign laws will not protect the intellectual property associated with The Chem-Mod Solution to the same extent as U.S. laws, leaving us vulnerable to companies outside the U.S. who may attempt to copy such intellectual property. In addition, other companies may make claims of intellectual property infringement with respect to The Chem-Mod Solution. Such intellectual property claims, with or without merit, could require that Chem-Mod (or us and our investment and operational partners) obtain a license to use the intellectual property, which might not be obtainable on favorable terms, if at all. On April 18, 2018, Nalco Company (which we refer to as Nalco) filed patent infringement lawsuits in the Western District of Wisconsin against two unaffiliated power plants that burn refined coal using the The Chem-Mod Solution. These complaints were filed following Nalco s voluntary dismissal of its action against Chem-Mod LLC and other defendants that was originally filed in the Northern District of Illinois in April 2014, as previously disclosed in our SEC filings. On July 16, 2018, Nalco amended its complaints to name as additional defendants in each case the refined coal limited liability company that sells refined coal to the power plant defendant in each case. The refined coal limited liability companies are licensed by Chem-Mod LLC to use the The Chem-Mod Solution to produce refined coal. The complaints allege that the named defendants infringe a patent licensed exclusively to Nalco and seek unspecified damages and injunctive relief. Although neither we nor Chem-Mod LLC is named as a defendant in either of these complaints, their defense was tendered to Chem-Mod LLC under certain agreements that provide for defense and indemnity, and those tenders were accepted. Chem-Mod LLC is directing the vigorous defense of these lawsuits. Litigation is inherently uncertain and, accordingly, it is not possible for us to predict the ultimate outcome of these matters. If Chem-Mod (or we and our investment and operational partners) cannot defeat or defend this or other such claims or obtain necessary licenses on reasonable terms, the operations may be precluded from using The Chem-Mod Solution.

Co-investor tax credit risks. We have co-investors in several of the operations currently producing refined coal. If in the future any one of our co-investors leaves a project, we could have difficulty finding replacements in a timely manner. On June 15, 2017, one of the refined coal partnerships in which we are an investor, received a notice from the IRS disallowing our co-investors from claiming tax credits. The position taken by the IRS has the potential to affect, and the IRS has opened audits of, other partnerships in which these co-investors are invested. However, the IRS notice does not challenge the validity of the tax credits themselves, or our ability to utilize tax credits. The partnership affected by the June 15, 2017 notice is defending its position in tax court. However, litigation is inherently uncertain and it is not possible to predict the ultimate outcome of this proceeding. An adverse ruling would likely make it more difficult for us to reach satisfactory arrangements with new co-investors and we may also be subject to claims against us from the co-investors affected by this IRS notice.

Operational risks. Chem-Mod s multi-pollutant reduction technologies (The Chem-Mod™ Solution) require chemicals that may not be readily available in the marketplace at reasonable costs. Utilities that use the technologies could be idled for various reasons, including operational or environmental problems at the plants or in the boilers, disruptions in the supply or transportation of coal, revocation of their Chem-Mod technologies environmental permits, labor strikes, force majeure events such as hurricanes, or terrorist attacks, any of which could halt or impede the operations. Long-term operations using Chem-Mod s multi-pollutant reduction technologies could also lead to unforeseen technical or other problems not evident in the short- or medium-term. A serious injury or death of a worker connected with the production of refined coal using Chem-Mod s technologies could expose the operations to material liabilities, jeopardizing our investment, and could lead to reputational harm. In the event of any such operational problems, we may not be able to take full advantage of the tax credits. We could also be exposed to risk due to our lack of control over the operations if future developments, for example a regulatory change affecting public and private companies differently, causes our interests and those of our co-investors to diverge. Finally, our vendors responsible for operation and management could fail to run the operations in compliance with IRC Section 45. If any of these developments occur, our investment returns may be negatively impacted.

Incompatible coal. If utilities purchase coal of a quality or type incompatible with their boilers and operations, treating such coal through a commercial refined coal plant could magnify the negative impacts of burning such coal. As a result, refined coal plants at such utilities may be removed from production until the incompatible coal has all been burned, which could cause us to be unable to take full advantage of the tax credits.

Strategic alternatives risk. While we currently expect to continue to hold at least a portion of our IRC Section 45 investments, if for any reason in the future we decide to sell more of our interests, the discount rate on future cash flows could be excessive, and could result in an impairment of our investment.

We began generating tax credits under IRC Section 45 in 2009. As of December 31, 2018, we had generated a total of $1,168 million ($1.168 billion) in IRC Section 45 tax credits, of which approximately $370 million have been used to offset U.S. federal tax liabilities and $798 million remain unused and available to offset future U.S. federal tax liabilities. Our ability to use tax credits under IRC Section 45 depends upon the operations in which we have invested satisfying certain ongoing conditions set forth in IRC Section 45. These include, among others, the placed-in-service condition and requirements relating to qualified emissions reductions, coal sales to unrelated parties and at least one of the operations owners qualifying as a producer of refined coal. While we have received some degree of confirmation from the IRS relating to our ability to claim these tax credits, the IRS could ultimately determine that the operations have not satisfied, or have not continued to satisfy, the conditions set forth in IRC Section 45. Similarly, the law permitting us to claim IRC Section 29 tax credits (related to our prior synthetic coal operations) expired on December 31, 2007. At December 31, 2018, we had exposure with respect to $108.0 million of previously earned tax credits under IRC Section 29. We believe our claim for IRC Section 29 tax credits in 2007 and prior years was in accordance with IRC Section 29 and four private letter rulings previously obtained by IRC Section 29-related limited liability companies in which we had an interest. We understand these private letter rulings were consistent with those issued to other taxpayers and we have received no indication from the IRS that it will seek to revoke or modify them. In addition, the IRS audited certain of the IRC Section 29 facilities without requiring any changes.

While none of our prior IRC Section 29 operations are currently under audit, many of the IRC Section 45 operations in which we are invested are under audit by the IRS. The IRS could place the remaining IRC Section 45 operations and any of the prior IRC Section 29 operations under audit. An adverse outcome with respect to our ability to claim tax credits under any such audit would likely cause a material loss or cause us to be subject to liability under indemnification obligations related to prior sales of partnership interests in IRC Section 29 tax credits.

The IRC Section 45 operations in which we have invested and the by-products from such operations may result in environmental and product liability claims and environmental compliance costs.

The construction and operation of the IRC Section 45 operations are subject to federal, state and local laws, regulations and potential liabilities arising under or relating to the protection or preservation of the environment, natural resources and human health and safety. Such laws and regulations generally require the operations and/or the utilities at which the operations are located to obtain and comply with various environmental registrations, licenses, permits, inspections and other approvals. There are costs associated with ensuring compliance with all applicable laws and regulations, and failure to fully comply with all applicable laws and regulations could lead to the imposition of penalties or other liability. Failure of The Chem-Mod Solution utilized at coal-fired generation facilities, for example, could result in violations of air emissions permits, which could lead to the imposition of penalties or other liability. Additionally, some environmental laws, without regard to fault or the legality of a party s conduct, on certain entities that are considered to have contributed to, or are otherwise responsible for, the release or threatened release of hazardous substances into the environment. One party may, under certain circumstances, be required to bear more than its share or the entire share of investigation and cleanup costs at a site if payments or participation cannot be obtained from other responsible parties. By using The Chem-Mod Solution at locations owned and operated by others, we and our partners may be exposed to the risk of being held liable for environmental damage from releases of hazardous substances we may have had little, if any, involvement in creating. Such risk remains even after production ceases at an operation to the extent the environmental damage can be traced to the types of chemicals or compounds used or operations conducted in connection with The Chem-Mod Solution. In addition, we and our partners could face the risk of environmental and product liability claims related to concrete incorporating fly ash produced using The Chem-Mod Solution. No assurances can be given that contractual arrangements and precautions taken to ensure assumption of these risks by facility owners or operators, or other end users, will result in that facility owner or operator, or other end user, accepting full responsibility for any environmental or product liability claim. Nor can we or our partners be certain that facility owners or operators, or other end users, will fully comply with all applicable laws and regulations, and this could result in environmental or product liability claims. It is also not uncommon for private claims by third parties alleging contamination to also include claims for personal injury, property damage, nuisance, diminution of property value, or similar claims. Furthermore, many environmental, health and safety laws authorize citizen suits, permitting third parties to make claims for violations of laws or permits. Our insurance may not cover all environmental risk and costs or may not provide sufficient coverage in the event of an environmental or product liability claim, and defense of such claims can be costly, even when such defense prevails. If significant uninsured losses arise from environmental or product liability claims, or if the costs of environmental compliance increase for any reason, our results of operations and financial condition could be adversely affected.

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We have debt outstanding that could adversely affect our financial flexibility and subjects us to restrictions and limitations that could significantly impact our ability to operate our business.

As of December 31, 2018, we had total consolidated debt outstanding of approximately $3.6 billion. The level of debt outstanding each period could adversely affect our financial flexibility. We also bear risk at the time our debt matures. Our ability to make interest and principal payments, to refinance our debt obligations and to fund our acquisition program and planned capital expenditures will depend on our ability to generate cash from operations. This, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control, such as an environment of rising interest rates. A small portion of our private placement debt consists of floating rate notes and interest payments under our senior revolving credit facility are based on a floating rate (in both cases currently based on LIBOR, which will transition soon to the Secured Overnight Financing Rate), which exposes us to additional risk in an environment of rising interest rates. Our indebtedness will also reduce the ability to use that cash for other purposes, including working capital, dividends to stockholders, acquisitions, capital expenditures, share repurchases, and general corporate purposes. If we cannot service our indebtedness, we may have to take actions such as selling assets, issuing additional equity or reducing or delaying capital expenditures, strategic acquisitions, and investments, any of which could impede the implementation of our business strategy or prevent us from entering into transactions that would otherwise benefit our business. Additionally, we may not be able to effect such actions, if necessary, on commercially reasonable terms, or at all. We may not be able to refinance any of our indebtedness on commercially reasonable terms, or at all.

The agreements governing our debt contain covenants that, among other things, restrict our ability to dispose of assets, incur additional debt, engage in certain asset sales, mergers, acquisitions or similar transactions, create liens on assets, engage in certain transactions with affiliates, change our business or make investments, and require us to comply with certain financial covenants. The restrictions in the agreements governing our debt may prevent us from taking actions that we believe would be in the best interest of our business and our stockholders and may make it difficult for us to execute our business strategy successfully or effectively compete with companies that are not similarly restricted. We may also incur future debt obligations that might subject us to additional or more restrictive covenants that could affect our financial and operational flexibility, including our ability to pay dividends. We cannot make any assurances that we will be able to refinance our debt or obtain additional financing on terms acceptable to us, or at all. A failure to comply with the restrictions under the agreements governing our debt could result in a default under the financing obligations or could require us to obtain waivers from our lenders for failure to comply with these restrictions. The occurrence of a default that remains uncured or the inability to secure a necessary consent or waiver could cause our obligations with respect to our debt to be accelerated and have a material adverse effect on our financial condition and results of operations.

We are a holding company and, therefore, may not be able to receive dividends or other distributions in needed amounts from our subsidiaries.

We are organized as a holding company, a legal entity separate and distinct from our operating subsidiaries. As a holding company without significant operations of our own, we are dependent upon dividends and other payments from our operating subsidiaries to meet our obligations for paying principal and interest on outstanding debt obligations, for paying dividends to stockholders, repurchasing our common stock and for corporate expenses. In the event our operating subsidiaries are unable to pay sufficient dividends and other payments to us, we may not be able to service our debt, pay our obligations, pay dividends on or repurchase our common stock.

Further, we derive a significant portion of our revenue and operating profit from operating subsidiaries located outside the U.S. Since the majority of financing obligations as well as dividends to stockholders are paid from the U.S., it is important to be able to access the cash generated by our operating subsidiaries located outside the U.S. in the event we are unable to meet these U.S. based cash requirements.

Funds from our operating subsidiaries outside the U.S. may be repatriated to the U.S. via stockholder distributions and intercompany financings, where necessary. A number of factors may arise that could limit our ability to repatriate funds or make repatriation cost prohibitive, including, but not limited to the imposition of currency controls and other government restrictions on repatriation in the jurisdictions in which our subsidiaries operate, fluctuations in foreign exchange rates, the imposition of withholding and other taxes on such payments and our ability to repatriate earnings in a tax-efficient manner.

In the event we are unable to generate or repatriate cash from our operating subsidiaries for any of the reasons discussed above, our overall liquidity could deteriorate and our ability to finance our obligations, including to pay dividends on or repurchase our common stock, could be adversely affected.

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Future sales or other dilution of our equity could adversely affect the market price of our common stock.

We grow our business organically as well as through acquisitions. One method of acquiring companies or otherwise funding our corporate activities is through the issuance of additional equity securities. The issuance of any additional shares of common or of preferred stock or convertible securities could be substantially dilutive to holders of our common stock. Moreover, to the extent that we issue restricted stock units, performance stock units, options or warrants to purchase shares of our common stock in the future and those options or warrants are exercised or as the restricted stock units or performance stock units vest, our stockholders may experience further dilution. Holders of our common stock have no preemptive rights that entitle holders to purchase their pro rata share of any offering of shares of any class or series and, therefore, such sales or offerings could result in increased dilution to our stockholders. The market price of our common stock could decline as a result of sales of shares of our common stock or the perception that such sales could occur.

The price of our common stock may fluctuate significantly, and this may make it difficult for you to resell shares of common stock owned by you at times or at prices you find attractive.

The trading price of our common stock may fluctuate widely as a result of a number of factors, including the risk factors described above, many of which are outside our control. In addition, the stock market is subject to fluctuations in the share prices and trading volumes that affect the market prices of the shares of many companies. These broad market fluctuations have adversely affected and may continue to adversely affect the market price of our common stock. Among the factors that could affect our stock price are:

- General economic and political conditions such as recessions, economic downturns and acts of war or terrorism;
- Quarterly variations in our operating results;
- Seasonality of our business cycle;
- Changes in the market s expectations about our operating results;
- Our operating results failing to meet the expectation of securities analysts or investors in a particular period;
- Changes in financial estimates and recommendations by securities analysts concerning us or the insurance brokerage or financial services industries in general;
- Operating and stock price performance of other companies that investors deem comparable to us;
- News reports relating to trends in our markets, including any expectations regarding an upcoming hard or soft market;
- Cyber attacks and other cybersecurity incidents;
- Changes in laws and regulations affecting our business;

- Material announcements by us or our competitors;
- The impact or perceived impact of developments relating to our investments, including the possible perception by securities analysts or investors that such investments divert management attention from our core operations;
- Market volatility;
- A negative market reaction to announced acquisitions;
- Competitive pressures in each of our segments;
- General conditions in the insurance brokerage and insurance industries;
- Legal proceedings or regulatory investigations;
- Regulatory requirements, including international sanctions and the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act 2010 or other anti-corruption laws;
- Quarter-to-quarter volatility in the earnings impact of IRC Section 45 tax credits from our clean energy investments, due to the application of accounting standards applicable to the recognition of tax credits; and
- Sales of substantial amounts of common shares by our directors, executive officers or significant stockholders or the perception that such sales could occur.

Stockholder class action lawsuits may be instituted against us following a period of volatility in our stock price. Any such litigation could result in substantial cost and a diversion of management s attention and resources.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

The executive offices of our corporate segment and certain subsidiary and branch facilities of our brokerage and risk management segments are located at 2850 Golf Road, Rolling Meadows, Illinois, where we own approximately 360,000 square feet of space, and can accommodate 2,000 employees at peak capacity.

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Elsewhere, we generally operate in leased premises related to the facilities of our brokerage and risk management operations. We prefer to lease office space rather than own real estate related to the branch facilities of our brokerage and risk management segments. Certain of our office space leases have options permitting renewals for additional periods. In addition to minimum fixed rentals, a number of our leases contain annual escalation clauses generally related to increases in an inflation index. See Note 16 to our 2018 consolidated financial statements for information with respect to our lease commitments as of December 31, 2018.

Item 3. Legal Proceedings.

Please see the information set forth in Note 16 to our consolidated financial statements, included herein, under Litigation, Regulatory and Taxation Matters.

Item 4. Mine Safety Disclosures.

Not applicable.

Executive Officers

Set forth below are the names, ages, positions and business backgrounds of our executive officers as of the date hereof:

Name	Age	Position and Year First Elected
J. Patrick Gallagher, Jr.	66	Chairman since 2006, President since 1990, Chief Executive Officer since 1995
Walter D. Bay	56	Corporate Vice President, General Counsel, Secretary since 2007
Richard C. Cary	56	Controller since 1997, Chief Accounting Officer since 2001
Joel D. Cavaness	57	Corporate Vice President since 2000, President of our Wholesale Brokerage Operation since 1997
Thomas J. Gallagher	60	Corporate Vice President since 2001, Chairman of our International Brokerage Operation 2010 - 2016, President of our Global Property/Casualty Brokerage Operation beginning in 2017
Douglas K. Howell	57	Corporate Vice President, Chief Financial Officer since 2003
Scott R. Hudson	57	Corporate Vice President and President of our Risk Management Operation since 2010
Christopher E. Mead	51	Corporate Vice President, Chief Marketing Officer since 2017; Managing Director Marketing Division, CME Group, 2005 - 2017
Susan E. Pietrucha	52	Corporate Vice President, Chief Human Resource Officer since 2007
William F. Ziebell	56	Corporate Vice President since 2011, regional leader in our Employee Benefit and Consulting Brokerage Operations 2004 - 2016, President beginning in 2017

We have employed each such person principally in management capacities for more than the past five years. All executive officers are appointed annually and serve at the pleasure of our board of directors.

Part II

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

Our common stock is listed on the New York Stock Exchange, trading under the symbol AJG.

As of January 31, 2019, there were approximately 1,000 holders of record of our common stock.

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(c) Issuer Purchases of Equity Securities

The following table shows the purchases of our common stock made by or on behalf of us or any affiliated purchaser (as such term is defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended) of us for each fiscal month in the three-month period ended December 31, 2018:

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share (2)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (3)	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs (3)
October 1 through October 31, 2018	2,499	$ 74.04		7,287,019
November 1 through November 30, 2018	754	77.86		7,287,019
December 1 through December 31, 2018	19,916	73.54		7,287,019
Total	23,169	$ 73.74		

(1) Amounts in this column include shares of our common stock purchased by the trustees of trusts established under our Deferred Equity Participation Plan (which we refer to as the DEPP), our Deferred Cash Participation Plan (which we refer to as the DCPP) and our Supplemental Savings and Thrift Plan (which we refer to as the Supplemental Plan), respectively. These plans are considered to be unfunded for purposes of federal tax law since the assets of these trusts are available to our creditors in the event of our financial insolvency. The DEPP is an unfunded, non-qualified deferred compensation plan that generally provides for distributions to certain of our key executives when they reach age 62 or upon or after their actual retirement. Under sub-plans of the DEPP for certain production staff, the plan generally provides for vesting and/or distributions no sooner than five years from the date of awards, although certain awards vest and/or distribute after the earlier of fifteen years or the participant reaching age 65. See Note 11 to our 2018 consolidated financial statements in this report for more information regarding the DEPP. The DCPP is an unfunded, non-qualified deferred compensation plan for certain key employees, other than executive officers, that generally provides for vesting and/or distributions no sooner than five years from the date of awards. Under the terms of the DEPP and the DCPP, we may contribute cash to the trust and instruct the trustee to acquire a specified number of shares of our common stock on the open market or in privately negotiated transactions. In the fourth quarter of 2018, we instructed the trustee for the DEPP and the DCPP to reinvest dividends on shares of our common stock held by these trusts and to purchase our common stock using cash that we contributed to the DCPP related to 2018 awards under the DCPP. The Supplemental Plan is an unfunded, non-qualified deferred compensation plan that allows certain highly compensated employees to defer compensation, including company match amounts, on a before-tax basis or after-tax basis. Under the terms of the Supplemental Plan, all amounts credited to an employee s account may be deemed invested, at the employee s election, in a number of investment options that include various mutual funds, an annuity product and a fund representing our common stock. When an employee elects to have some or all of the amounts credited to the employee s account under the Supplemental Plan deemed to be invested in the fund representing our common stock, the trustee of the trust for the Supplemental Plan purchases shares of our common stock in a number sufficient to ensure that the trust holds a number of shares of our common stock with a value equal to all equivalent to the amounts deemed invested in the fund representing our common stock. We want to ensure that at the time when an employee becomes entitled to a distribution under the terms of the Supplemental Plan, any amounts deemed to be invested in the fund representing our common stock are distributed in the form of shares of our common stock held by the trust. We established the trusts for the DEPP, the DCPP and the Supplemental Plan to assist us in discharging our deferred compensation obligations under these plans. All assets of these trusts, including any shares of our common stock purchased by the trustees, remain, at all times, assets of the Company, subject to the claims of our creditors in the event of our financial insolvency. The terms of the DEPP, the DCPP and the Supplemental Plan do not provide for a specified limit on the number of shares of common stock that may be purchased by the respective trustees of the trusts.

(2) The average price paid per share is calculated on a settlement basis and does not include commissions.

(3)

We have a common stock repurchase plan that the board of directors adopted on May 10, 1988 and has periodically amended since that date to authorize additional shares for repurchase (the last amendment was on January 24, 2008 and approved the repurchase of 10,000,000 shares). The repurchase plan has no expiration date and we are under no commitment or obligation to repurchase any particular amount of our common stock under the plan. At our discretion, we may suspend the repurchase plan at any time.

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Item 6. Selected Financial Data.

The following selected consolidated financial data for each of the five years in the period ended December 31, 2018 have been derived from our consolidated financial statements. Such data should be read in conjunction with our consolidated financial statements and notes thereto in Item 8 of this annual report.

	Year Ended December 31,				
	2018	2017 As Restated*	2016 As Restated*	2015	2014
	(In millions, except per share and employee data)				
Consolidated Statement of Earnings Data:					
Commissions	$ 2,920.7	$ 2,641.0	$ 2,409.9	$ 2,338.7	$ 2,083.0
Fees	1,756.3	1,591.9	1,491.7	1,432.3	1,258.3
Supplemental revenues	189.9	158.0	139.9	125.5	104.0
Contingent revenues	98.0	99.5	97.9	93.7	84.7
Investment income and other	1,827.5	1,622.6	1,409.0	1,402.2	1,096.5
Revenue before reimbursements	6,792.4	6,113.0	5,548.4	5,392.4	4,626.5
Reimbursements	141.6	136.0	132.1		
Total revenues	6,934.0	6,249.0	5,680.5	5,392.4	4,626.5
Total expenses	6,454.6	5,889.2	5,346.9	5,098.9	4,335.0
Earnings before income taxes	479.4	359.8	333.6	293.5	291.5
Provision (benefit) for income taxes	(196.5)	(157.1)	(96.7)	(95.6)	(36.0)
Net earnings	675.9	516.9	430.3	389.1	327.5
Net earnings attributable to noncontrolling interests	42.4	35.6	33.5	32.3	24.1
Net earnings attributable to controlling interests	$ 633.5	$ 481.3	$ 396.8	$ 356.8	$ 303.4
Per Share Data:					
Diluted net earnings per share (1)	3.40	2.64	2.22	2.06	1.97
Dividends declared per common share (2)	1.64	1.56	1.52	1.48	1.44
Share Data:					
Shares outstanding at year end	184.0	181.0	178.3	176.9	164.6
Weighted average number of common shares outstanding	182.7	180.1	177.6	172.2	152.9
Weighted average number of common and common equivalent shares outstanding	186.2	182.1	178.4	173.2	154.3
Consolidated Balance Sheet Data:					
Total assets	$ 16,334.0	$ 14,909.7	$ 13,528.2	$ 10,910.5	$ 10,010.0
Long-term debt less current portion	3,098.0	2,698.0	2,150.0	2,075.0	2,125.0
Total stockholders equity	4,569.7	4,299.7	3,775.5	3,688.2	3,305.1
Return on beginning stockholders equity (3)	15%	13%	11%	11%	14%
Employee Data:					
Number of employees - at year end	30,362	26,783	24,790	23,857	22,375

(1) Based on the weighted average number of common and common equivalent shares outstanding during the year.
(2) Based on the total dividends declared on a share of common stock outstanding during the entire year.
(3) Represents net earnings divided by total stockholders equity, as of the beginning of the year.
* See Note 3 Revenues from Contracts with Customers for additional information about the restatements related to Topic 606. We adopted Topic 606 as of January 1, 2018, using the full retrospective method to restate 2017 and 2016. The cumulative effect of the adoption was

recognized as an increase to retained earnings of $125.3 million on January 1, 2016. As permitted under the guidelines issued by the SEC related to the adoption of Topic 606, we did not restate the 2015 and 2014 information in the table above.

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

Introduction

The following discussion and analysis should be read in conjunction with our consolidated financial statements and the related notes included in Item 8 of this annual report. In addition, please see Information Regarding Non-GAAP Measures and Other beginning on page 32 for a reconciliation of the non-GAAP measures for adjusted total revenues, organic commission, fee and supplemental revenues and adjusted EBITDAC to the comparable GAAP measures, as well as other important information regarding these measures.

We are engaged in providing insurance brokerage and consulting services, and third-party property/casualty claims settlement and administration services to entities in the U.S. and abroad. We believe that one of our major strengths is our ability to deliver comprehensively structured insurance and risk management services to our clients. Our brokers, agents and administrators act as intermediaries between underwriting enterprises and our clients and we do not assume net underwriting risks. We are headquartered in Rolling Meadows, Illinois, have operations in 35 other countries and offer client-service capabilities in more than 150 countries globally through a network of correspondent brokers and consultants. In 2018, we expanded, and expect to continue to expand, our international operations through both acquisitions and organic growth. We generate approximately 70% of our revenues for the combined brokerage and risk management segments domestically, with the remaining 30% derived internationally, primarily in Australia, Bermuda, Canada, the Caribbean, New Zealand and the U.K. (based on 2018 revenues). We expect that our international revenue as a percentage of our total revenues in 2019 will be comparable to 2018. We have three reportable segments: brokerage, risk management and corporate, which contributed approximately 61%, 14% and 25%, respectively, to 2018 revenues. Our major sources of operating revenues are commissions, fees and supplemental and contingent revenues from brokerage operations and fees from risk management operations. Investment income is generated from invested cash and fiduciary funds, clean energy investments, and interest income from premium financing.

This Management s Discussion and Analysis of Financial Condition and Results of Operations contains certain statements relating to future results which are forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. Please see Information Concerning Forward-Looking Statements at the beginning of this annual report, for certain cautionary information regarding forward-looking statements and a list of factors that could cause our actual results to differ materially from those predicted in the forward-looking statements.

Accounting Changes - Impact of New Revenue Recognition Accounting Standard

As a result of adopting a new revenue recognition accounting statement, we restated our consolidated financial statements and related information from amounts previously reported herein for 2017 and 2016. Notes 2 and 3 to our 2018 consolidated financial statements included in this report contains information regarding the impact the new revenue recognition accounting standard had on our financial presentation. We adopted the new standard as of January 1, 2018, using the full retrospective method to restate each prior reporting period presented. The cumulative effect of the adoption was an increase to retained earnings of $125.3 million as of January 1, 2016. While the adoption of the new standard did not have a material impact on the presentation of our consolidated results of operations on an annual basis, there was a material impact on the presentation of our results in certain quarters due to timing changes in the recognition of certain revenue and expenses. As a result, we did experience a different seasonality in our quarterly results after adoption of the new standard, with a shift in the timing of revenue recognized from the second, third and fourth quarters to the first quarter.

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Summary of Financial Results - Year Ended December 31,

See the reconciliations of non-GAAP measures on pages 28 and 29.

	Year 2018		Year 2017		Change	
	Reported GAAP	Adjusted Non-GAAP	Reported GAAP	Adjusted Non-GAAP	Reported GAAP	Adjusted Non-GAAP
			(In millions, except per share data)			
Brokerage Segment						
Revenues	$ 4,246.9	$ 4,236.7	$ 3,815.1	$ 3,824.7	11%	11%
Organic revenues		$ 3,960.2		$ 3,749.0		5.6%
Net earnings	$ 573.2		$ 414.7		38%	
Net earnings margin	13.5%		10.9%		+263 bpts	
Adjusted EBITDAC		$ 1,172.4		$ 1,043.0		12%
Adjusted EBITDAC margin		27.7%		27.3%		+40 bpts
Diluted net earnings per share	$ 3.02	$ 3.24	$ 2.23	$ 2.50	35%	30%
Risk Management Segment						
Revenues	$ 798.3	$ 798.3	$ 737.4	$ 734.7	8%	9%
Organic revenues		$ 786.3		$ 734.2		7.1%
Net earnings	$ 70.4		$ 55.7		26%	
Net earnings margin (before reimbursements)	8.8%		7.6%		+127 bpts	
Adjusted EBITDAC		$ 138.7		$ 126.1		10%
Adjusted EBITDAC margin (before reimbursements)		17.4%		17.2%		+21 bpts
Diluted net earnings per share	$ 0.38	$ 0.37	$ 0.31	$ 0.32	23%	16%
Corporate Segment						
Diluted net earnings (loss) per share	$	$ (0.16)	$ 0.10	$ 0.18		