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Audited Consolidated Financial Statements

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
EVERTEC, Inc.

We have audited the accompanying consolidated balance sheets of EVERTEC, Inc. and subsidiaries (the “Company”) as of December 31, 2016 and 2015, and the related consolidated statements of income and comprehensive income, changes in stockholders’ equity, and cash flows for each of the two years in the period ended December 31, 2016. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of EVERTEC, Inc. and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2016, based on the criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 24, 2017 expressed an unqualified opinion on the Company’s internal control over financial reporting.

/s/ Deloitte & Touche LLP

San Juan, Puerto Rico
February 24, 2017
Stamp No. E242693
affixed to original

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of EVERTEC, Inc.

In our opinion, the consolidated statement of income and comprehensive income, of changes in stockholders' equity and of cash flows for the year ended December 31, 2014, present fairly, in all material respects, the results of operations and cash flows of EVERTEC, INC. and its subsidiaries for the year ended December 31, 2014, in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15 (a) (2) for the year ended December 31, 2014 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audit. We conducted our audit of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

San Juan, Puerto Rico

March 2, 2015, except for the effects of the restatement discussed in Note 1 (not presented herein) to the consolidated financial statements appearing under Item 8 of the Company's 2015 annual report on Form 10-K and the effect of the restatement discussed in Note 1 (not presented herein) to the financial statement schedule appearing under Item 15 (a) (2) of the Company's 2015 annual report on Form 10-K, as to which the date is May 26, 2016

CERTIFIED PUBLIC ACCOUNTANTS (OF PUERTO RICO)

License No. LLP-216 Expires Dec. 1, 2019

Stamp E257025 of the Puerto Rico Society of Certified Public Accountants has been affixed to the file copy of this report

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
EVERTEC, Inc.

We have audited the internal control over financial reporting of EVERTEC, Inc. and subsidiaries (the “Company”) as of December 31, 2016, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company’s internal control over financial reporting is a process designed by, or under the supervision of, the company’s principal executive and principal financial officers, or persons performing similar functions, and effected by the company’s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedule as of and for the year ended December 31, 2016, of the Company and our report dated February 24, 2017 expressed an unqualified opinion on those financial statements and financial statement schedule.

/s/ Deloitte & Touche LLP

San Juan, Puerto Rico
February 24, 2017
Stamp No. E242694
affixed to Original

EVERTEC, Inc. Consolidated Balance Sheets
(Dollar amounts in thousands, except share data)

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
Assets		
Current Assets:		
Cash	\$ 51,920	\$ 28,747
Restricted cash	8,112	11,818
Accounts receivable, net	77,803	73,715
Deferred tax asset	—	1,685
Prepaid expenses and other assets	<u>20,430</u>	<u>18,758</u>
Total current assets	158,265	134,723
Investment in equity investee	12,252	12,264
Property and equipment, net	38,930	34,128
Goodwill	370,986	368,133
Other intangible assets, net	299,119	312,059
Long-term deferred tax asset	805	—
Other long-term assets	<u>5,305</u>	<u>2,347</u>
Total assets	<u>\$885,662</u>	<u>\$863,654</u>
Liabilities and stockholders' equity		
Current Liabilities:		
Accrued liabilities	\$ 34,243	\$ 37,308
Accounts payable	40,845	21,216
Unearned income	4,531	2,877
Income tax payable	1,755	1,350
Current portion of long-term debt	19,789	22,750
Short-term borrowings	<u>28,000</u>	<u>17,000</u>
Total current liabilities	129,163	102,501
Long-term debt	599,667	619,297
Long-term deferred tax liability	14,978	20,614
Unearned income—long-term	17,303	10,939
Other long-term liabilities	<u>16,376</u>	<u>12,089</u>
Total liabilities	<u>777,487</u>	<u>765,440</u>
Commitments and contingencies (Notes 18 and 21)		
Stockholders' equity		
Preferred stock, par value \$0.01; 2,000,000 shares authorized; none issued	—	—
Common stock, par value \$0.01; 206,000,000 shares authorized; 72,635,032 shares issued and outstanding at December 31, 2016 (December 31, 2015—74,988,210)	726	750
Additional paid-in capital	—	9,718
Accumulated earnings	116,341	95,328
Accumulated other comprehensive loss, net of tax	<u>(12,391)</u>	<u>(7,582)</u>
Total EVERTEC, Inc stockholders' equity	104,676	98,214
Non-controlling interest	<u>3,499</u>	<u>—</u>
Total equity	<u>108,175</u>	<u>98,214</u>
Total liabilities and stockholders' equity	<u>\$885,662</u>	<u>\$863,654</u>

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

EVERTEC, Inc. Consolidated Statements of Income and Comprehensive Income
(Dollar amounts in thousands, except per share data)

	Years ended December 31,		
	2016	2015	2014
Revenues			
Merchant Acquiring, net	\$ 91,248	\$ 85,411	\$ 79,136
Payment Processing (from affiliates: \$32,485, \$30,504 and \$27,094)	111,507	108,320	104,713
Business Solutions (from affiliates: \$143,988, \$138,929 and \$137,242)	186,752	179,797	177,939
Total revenues	<u>389,507</u>	<u>373,528</u>	<u>361,788</u>
Operating costs and expenses			
Cost of revenues, exclusive of depreciation and amortization shown below	175,809	167,916	157,537
Selling, general and administrative expenses	46,986	37,278	41,276
Depreciation and amortization	59,567	64,974	65,988
Total operating costs and expenses	<u>282,362</u>	<u>270,168</u>	<u>264,801</u>
Income from operations	<u>107,145</u>	<u>103,360</u>	<u>96,987</u>
Non-operating income (expenses)			
Interest income	377	495	328
Interest expense	(24,617)	(24,266)	(25,772)
(Losses) earnings of equity method investment	(52)	147	1,140
Other income, net	544	2,306	2,375
Total non-operating expenses	<u>(23,748)</u>	<u>(21,318)</u>	<u>(21,929)</u>
Income before income taxes	<u>83,397</u>	<u>82,042</u>	<u>75,058</u>
Income tax expense (benefit)	<u>8,271</u>	<u>(3,335)</u>	<u>8,901</u>
Net income	<u>75,126</u>	<u>85,377</u>	<u>66,157</u>
Less: Net income attributable to non-controlling interest	<u>90</u>	<u>—</u>	<u>—</u>
Net income attributable to EVERTEC, Inc.'s common stockholders	<u>75,036</u>	<u>85,377</u>	<u>66,157</u>
Other comprehensive (loss) income, net of tax of \$176, \$8 and \$4	.	.	.
Foreign currency translation adjustments	(3,360)	(545)	(6,948)
Loss on cash flow hedge	(1,449)	(515)	—
Total comprehensive income attributable to EVERTEC, Inc.'s common stockholders	<u>\$ 70,227</u>	<u>\$ 84,317</u>	<u>\$ 59,209</u>
Net income per common share—basic attributable to EVERTEC, Inc.'s common stockholders	<u>\$ 1.01</u>	<u>\$ 1.11</u>	<u>\$ 0.84</u>
Net income per common share—diluted attributable to EVERTEC, Inc.'s common stockholders	<u>\$ 1.01</u>	<u>\$ 1.11</u>	<u>\$ 0.84</u>
Cash dividends declared per share	<u>\$ 0.40</u>	<u>\$ 0.40</u>	<u>\$ 0.40</u>

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

EVERTEC, Inc. Consolidated Statements of Changes in Stockholders' Equity
(Dollar amounts in thousands, except share data)

	Number of Shares of Common Stock	Common Stock	Additional Paid-in Capital	Accumulated Earnings	Accumulated Other Comprehensive (Loss) Income	Non-Controlling Interest	Total Stockholders' Equity
Balance at December 31, 2013	78,286,465	\$ 783	\$ 80,718	\$ 6,045	\$ 426	\$ —	\$ 87,972
Share-based compensation recognized	—	—	4,587	—	—	—	4,587
Tax windfall benefit on share-based compensation	—	—	3,669	—	—	—	3,669
Stock options exercised, net of cashless exercise	799,885	8	(1,440)	—	—	—	(1,432)
Restricted stock units delivered	7,988	—	(26)	—	—	—	(26)
Repurchase of common stock	(1,201,194)	(12)	(26,185)	—	—	—	(26,197)
Net income	—	—	—	66,157	—	—	66,157
Dividend ⁽¹⁾	—	—	21	—	—	—	21
Cash dividends paid on common stock	—	—	—	(31,359)	—	—	(31,359)
Cash settlement of stock options	—	—	(1,604)	—	—	—	(1,604)
Other comprehensive loss	—	—	—	—	(6,948)	—	(6,948)
Balance at December 31, 2014	77,893,144	779	59,740	40,843	(6,522)	—	94,840
Share-based compensation recognized	—	—	5,204	—	—	—	5,204
Repurchase of common stock	(3,012,826)	(30)	(54,919)	—	—	—	(54,949)
Restricted stock grants and units delivered, net of cashless exercise	107,892	1	(307)	—	—	—	(306)
Net income	—	—	—	85,377	—	—	85,377
Cash dividends declared on common stock	—	—	—	(30,892)	—	—	(30,892)
Other comprehensive loss	—	—	—	—	(1,060)	—	(1,060)
Balance at December 31, 2015	74,988,210	750	9,718	95,328	(7,582)	—	98,214
Share-based compensation recognized	—	—	6,408	—	—	—	6,408
Repurchase of common stock	(2,504,427)	(25)	(15,594)	(24,327)	—	—	(39,946)
Stock options exercised, net of cashless exercise	8,393	—	(79)	—	—	—	(79)
Restricted stock grants and units delivered, net of cashless	142,856	1	(471)	—	—	—	(470)
Net income	—	—	—	75,036	—	90	75,126
Non-controlling interest on acquisition	—	—	—	—	—	3,409	3,409
Cash dividends declared on common stock	—	—	—	(29,696)	—	—	(29,696)
Dividend reversal for forfeited options	—	—	18	—	—	—	18
Other comprehensive loss	—	—	—	—	(4,809)	—	(4,809)
Balance at December 31, 2016	72,635,032	\$ 726	\$ —	\$ 116,341	\$(12,391)	\$ 3,499	\$ 108,175

⁽¹⁾ Related to dividend declared in 2012 and accrued upon vesting of stock options. Such options were forfeited during 2014.

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

EVERTEC, Inc. Consolidated Statements of Cash Flows
(Dollar amounts in thousands)

	Years ended December 31,		
	2016	2015	2014
Cash flows from operating activities			
Net income	\$ 75,126	\$ 85,377	\$ 66,157
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	59,567	64,974	65,988
Amortization of debt issue costs and accretion of discount	4,334	3,329	3,094
Loss on extinguishment of debt	1,476	—	—
Provision for doubtful accounts and sundry losses	1,990	2,130	1,360
Deferred tax benefit	(4,594)	(3,090)	(3,701)
Share-based compensation	6,408	5,204	4,587
Loss on disposal of property and equipment and other intangibles	453	143	734
Loss on impairment of software	2,277	—	—
Losses (earnings) of equity method investment	52	(147)	(1,140)
Dividend received from equity method investment	—	—	326
(Increase) decrease in assets:			
Accounts receivable, net	(2,583)	(4,482)	(5,587)
Prepaid expenses and other assets	(1,426)	(146)	65
Other long-term assets	(1,790)	(70)	3,365
Increase (decrease) in liabilities:			
Accounts payable and accrued liabilities	14,594	15,947	(3,925)
Income tax payable	405	(606)	1,697
Unearned income	8,018	2,207	3,571
Other long-term liabilities	3,747	(8,351)	3,228
Total adjustments	92,928	77,042	73,662
Net cash provided by operating activities	168,054	162,419	139,819
Cash flows from investing activities			
Net decrease (increase) in restricted cash	3,705	(6,100)	(285)
Additions to software and purchase of customer relationship	(23,819)	(25,960)	(14,707)
Acquisitions, net of cash acquired	(15,600)	—	—
Property and equipment acquired	(18,450)	(21,022)	(10,898)
Proceeds from sales of property and equipment	81	14	59
Net cash used in investing activities	(54,083)	(53,068)	(25,831)
Cash flows from financing activities			
Proceeds from issuance of long-term debt	75,763	—	—
Debt issuance costs	(4,830)	—	—
Net increase (decrease) in short-term borrowings	11,000	(6,000)	(27,000)
Repayments of borrowings for purchase of equipment and software	(2,213)	(1,542)	(1,200)
Dividends paid	(29,696)	(30,921)	(31,359)
Statutory minimum withholding taxes paid on share-based compensation	(548)	(306)	(2,001)
Tax windfall benefits on share-based compensation	—	—	3,669
Issuance of common stock	—	—	543
Repurchase of common stock	(39,946)	(54,949)	(26,197)
Settlement of stock options	—	—	(1,604)
Repayment of long-term debt	(96,741)	(19,000)	(19,000)
Credit amendment fees	(3,587)	—	—
Net cash used in financing activities	(90,798)	(112,718)	(104,149)
Net increase (decrease) in cash	23,173	(3,367)	9,839
Cash at beginning of the period	28,747	32,114	22,275
Cash at end of the period	\$ 51,920	\$ 28,747	\$ 32,114
Supplemental disclosure of cash flow information:			
Cash paid for interest	\$ 22,535	\$ 21,497	\$ 24,280
Cash paid for income taxes	8,697	5,682	976
Supplemental disclosure of non-cash activities:			
Payable due to vendor related to property and equipment and software acquired	3,302	3,638	6,115

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

Notes to Audited Consolidated Financial Statements

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EVERTEC, Inc. Notes to Consolidated Financial Statements

Note 1—The Company and Summary of Significant Accounting Policies

The Company

EVERTEC, Inc. (formerly known as Carib Latam Holdings, Inc.) and its subsidiaries (collectively the “Company,” or “EVERTEC”) is a leading full-service transaction processing business in Latin America and the Caribbean. The Company is based in Puerto Rico and provides a broad range of merchant acquiring, payment processing and business process management services across 18 countries in the region. EVERTEC owns and operates the ATH network, one of the leading automated teller machine (“ATM”) and personal identification number (“PIN”) debit networks in Latin America. In addition, EVERTEC provides a comprehensive suite of services for core bank processing, cash processing and technology outsourcing in the regions the Company serves. EVERTEC serves a broad and diversified customer base of leading financial institutions, merchants, corporations and government agencies with solutions that are essential to their operations, enabling them to issue, process and accept transactions securely.

Initial Public Offering and Other Public Offerings

On April 17, 2013, the Company completed its initial public offering of 28,789,943 shares of common stock at a price to the public of \$20.00 per share. On September 18, 2013 and December 13, 2013, the Company completed public offerings of 23,000,000 and 15,233,273 shares, respectively, of the Company’s common stock by Apollo Global Management, LLC (“Apollo”), Popular, Inc. (“Popular”), and current and former employees. After the completion of these offerings, Popular owned approximately 11.7 million shares of EVERTEC’s common stock, or 16.05% as of December 31, 2016, and Apollo no longer owns any of the Company’s common stock.

Basis of Presentation

The consolidated financial statements of EVERTEC have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). In the opinion of management, the accompanying consolidated financial statements, prepared in accordance with GAAP, contain all adjustments, all of which are normal and recurring in nature, necessary for a fair presentation.

A summary of the most significant accounting policies used in preparing the accompanying consolidated financial statements is as follows:

Principles of Consolidation

The accompanying consolidated financial statements include the accounts and operations of the Company, which are presented in accordance with GAAP. The Company consolidates all entities that are controlled by ownership of a majority voting interest. Intercompany accounts and transactions are eliminated in the consolidated financial statements.

Use of Estimates

The preparation of the accompanying consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period.

Revenue Recognition

The Company’s revenue recognition policy follows the guidance from Accounting Standards Codification (“ASC”) 605 *Revenue Recognition*; ASC 605-25, *Revenue Recognition—Multiple Element Arrangements*; and; ASC 985, *Software*, which provide guidance on the recognition, presentation, and disclosure of revenue in consolidated financial statements.

EVERTEC, Inc. Notes to Consolidated Financial Statements

The Company recognizes revenue when the following four criteria are met: (i) persuasive evidence of an agreement exists, (ii) delivery and acceptance has occurred or services have been rendered, (iii) the selling price is fixed or determinable, and (iv) collection is reasonably assured. For multiple deliverable arrangements, EVERTEC evaluates each arrangement to determine if the elements or deliverables within the arrangement represent separate units of accounting pursuant to ASC 605-25. If the deliverables are determined to be separate units of accounting, revenues are recognized as units of accounting are delivered and the revenue recognition criteria are met. If the deliverables are not determined to be separate units of accounting, revenues for the delivered services are combined into one unit of accounting and recognized (i) over the life of the arrangement if all services are consistently delivered over such term, or if otherwise, (ii) at the time that all services and deliverables have been delivered. The selling price for each deliverable is based on vendor specific objective evidence (“VSOE”) if available, third party evidence (“TPE”) if VSOE is not available, or management best estimate of selling price (“BESP”) if neither VSOE nor TPE is available. EVERTEC establishes VSOE of selling price using the price charged when the same element is sold separately. EVERTEC bifurcates or allocates the arrangement consideration to each of the deliverables based on the relative selling price of each unit of accounting.

The Company has two main categories of revenues according to the type of transactions EVERTEC enters into with the Company’s customers: (a) transaction-based fees and (b) fixed fees and time and material.

Transaction-based fees

The Company provides services that generate transaction-based fees. Typically transaction-based fees depend on factors such as number of accounts or transactions processed. These factors typically consist of a fee per transaction or item processed, a percentage of dollar volume processed or a fee per account on file, or some combination thereof. Revenue derived from the transaction-based fee contracts are recognized when the underlying transaction is processed, which constitutes delivery of service.

Revenues from business contracts in the Company’s Merchant Acquiring segment are primarily comprised of discount fees charged to the merchants based on the sales amount of transactions processed. Revenues include a discount fee and membership fees charged to merchants and debit network fees as well as point-of-sale (“POS”) rental fees. Pursuant to the guidance from ASC 605-45-45, *Revenue Recognition—Principal Agent Considerations*, EVERTEC records Merchant Acquiring revenues net of interchange and assessments charged by the credit and debit card network associations and recognizes such revenues at the time of the sale (when a transaction is processed).

Payment processing revenues are comprised of revenues related to providing access to the ATH network and other card networks to financial institutions, and related services. Payment processing revenues also include revenues from card issuer processing services (such as credit and debit card processing, authorization and settlement, and fraud monitoring and control to debit or credit card issuers), payment processing services (such as payment and billing products for merchants, businesses and financial institutions) and electronic benefit transfer (“EBT”) (which principally consists of services to the Puerto Rico government for the delivery of government benefits to participants). Revenues in EVERTEC’s Payment Processing segment are primarily comprised of fees per transaction processed or per account on file, or a combination of both, and are recognized at the time transactions are processed or on a monthly basis for accounts on file.

Transaction-based fees within EVERTEC’s Business Solutions segment consist of revenues from business process management solutions including core bank processing, business process outsourcing, item and cash processing, and fulfillment. Transaction-based fee revenues generated by the Company’s core bank processing services are derived from fees based on various factors such as the number of accounts on file (e.g. savings or checking accounts, loans, etc.), and the number of transactions processed or registered users (e.g. for online

EVERTEC, Inc. Notes to Consolidated Financial Statements

banking services). For services dependent on the number of transactions processed, revenues are recognized as the underlying transactions are processed. For services dependent on the number of users or accounts on file, revenues are recognized on a monthly basis based on the number of accounts on file each month. Item and cash processing revenues are based upon the number of items (e.g. checks) processed and revenues are recognized when the underlying item is processed. Fulfillment services include technical and operational resources for producing and distributing variable print documents such as statements, bills, checks and benefits summaries. Fulfillment revenues are based upon the number pages for printing services and the number of envelopes processed for mailing services. Revenues are recognized as services are delivered based on a fee per page printed or envelope mailed, as applicable.

Fixed fees and time and material

The Company also provides services that generate a fixed fee per month or fees based on time and expenses incurred. These services are mostly provided in EVERTEC's Business Solutions segment. Revenues are generated from EVERTEC's core bank solutions, network hosting and management and IT consulting services.

In core bank solutions, the Company mostly provides access to applications and services such as back-up or recovery, hosting and maintenance that enable a bank to operate the related hosted services accessing the Company's IT infrastructure. These contracts generally contain multiple elements or deliverables which are evaluated by EVERTEC and revenues are recognized according to the applicable guidance. Revenue is derived from fixed fees charged for the use of hosted services and are recognized on a monthly basis as delivered. Set-up fees are billed to the customer when the service is rendered; however, they are deferred and recognized as revenues over the term of the arrangement or the expected period of the customer relationship, whichever is longer, as set-up services rarely provide value to the customer on a stand-alone basis and are interrelated with the service to be provided under the contract.

In network hosting and management, EVERTEC provides hosting services for network infrastructure at EVERTEC's facilities; automated monitoring services; maintenance of call centers; interactive voice response solutions, among other related services. Revenues are primarily derived from monthly fees as services are delivered. Set-up fees are billed up-front to the customer when the set-up service is rendered; however, they are deferred and recognized as revenues over the term of the arrangement or the expected period of the customer relationship, whichever is longer, as set-up services rarely provide value to the customer on a stand-alone basis and are interrelated with the service under the contract. There are some arrangements under this line of service category that may contain undelivered elements. In such cases, the undelivered elements are evaluated and recognized when the services are delivered or at the time that all deliverables under the contract have been delivered.

IT consulting services revenue primarily consists of time billings based upon the number of hours dedicated to each client. Revenue from time billings are recognized as services are delivered.

EVERTEC also charges members of the ATH network an annual membership fee; however, these fees are deferred and recognized as revenues on a straight-line basis over the year and recorded in the Company's Payment Processing segment. In addition, occasionally EVERTEC is a reseller of hardware and software products and revenues from these resale transactions are recognized when such product is delivered and accepted by the client.

Service level arrangements

The Company's service contracts may include service level arrangements ("SLA") generally allowing the customer to receive a credit for part of the service fee when the Company has not provided the agreed level of

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services. The SLA performance obligation is committed on a monthly basis, thus SLA performance is monitored and assessed for compliance with arrangements on a monthly basis, including determination and accounting for its economic impact, if any.

Investment in Equity Investee

The Company accounts for investments using the equity method of accounting if the investment provides the Company the ability to exercise significant influence, but not control, over an investee. Significant influence is generally deemed to exist if the Company has an ownership interest in the voting stock of an investor of between 20 percent and 50 percent, although other factors are considered in determining whether the equity method of accounting is appropriate. Under this method, the investment, originally recorded at cost, is adjusted to recognize the Company's share of net income or losses as they occur. The Company's share of investee earnings or losses is recorded, net of taxes, within earnings of equity method investment caption in the consolidated statements of income and comprehensive income. The Company's consolidated revenues include fees for services provided to an investee accounted for under the equity method. Additionally, the Company's interest in the net asset of its equity method investee is reflected in the consolidated balance sheets. On the acquisition of the investment any difference between the cost of the investment and the amount of the underlying equity in net assets of an investee is required to be accounted as if the investee were a consolidated subsidiary. If the difference is assigned to depreciable or amortizable assets or liabilities, then the difference should be amortized or accreted in connection with the equity earnings based on the Company's proportionate share of the investee's net income or loss. If the investor is unable to relate the difference to specific accounts of the investee, the difference should be considered to be goodwill.

The Company considers whether the fair value of its equity method investment has declined below their carrying value whenever adverse events or changes in circumstances indicate that recorded values may not be recoverable. If the Company considered any such decline to be other than temporary (based on various factors, including historical financial results, product development activities and the overall health of the investee's industry), then the Company would record a write-down to estimated fair value.

Property and Equipment

Property and equipment are stated at cost, net of accumulated depreciation and amortization. Depreciation of property and equipment is computed using the straight-line method and expensed over their estimated useful lives. Amortization of leasehold improvements is computed over the terms of the respective leases, including renewal options considered by management to be reasonably assured of being exercised, or the estimated useful lives of the improvements, whichever is shorter. Costs of maintenance and repairs which do not improve or extend the life of the respective assets are expensed as incurred.

Impairment on Long-lived Assets

Long-lived assets to be held and used, and long-lived assets to be disposed of, are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Capitalization of Software

EVERTEC Group LLC's ("EVERTEC Group"), EVERTEC's main operating subsidiary, develops software that is used in providing processing services to customers. Capitalized software includes purchased software and internally-developed software and is recognized as software packages within the other intangible assets line item in the consolidated balance sheets. Capitalization of internally developed software occurs only after the preliminary project stage is complete and technological feasibility has been achieved, and management's

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estimation that the likelihood of successful development and implementation reaches a provable level. Tasks that are generally capitalized are as follows: (a) system design of a chosen path including software configuration and software interfaces; (b) employee costs directly associated with the internal-use computer software project; (c) software development (coding) and software and system testing and verification; (d) system installation; and (e) enhancements that add function and are considered permanent. These tasks are capitalized and amortized using the straight line method over its estimated useful life, which range from three to ten years and is included in depreciation and amortization in the consolidated statements of income and comprehensive income.

The Company capitalizes interest costs incurred in the development of software. The amount of interest capitalized is an allocation of the interest cost incurred during the period required to substantially complete the asset. The interest rate for capitalization purposes is based on a weighted average rate on the Company's outstanding borrowing. For the years ended December 31, 2016, 2015 and 2014, interest cost capitalized amounted to approximately \$0.4 million, \$0.3 million and \$0.3 million, respectively.

Software and Maintenance Contracts

Software and maintenance contracts are recorded at cost. Amortization of software and maintenance contracts is computed using the straight-line method and expensed over their estimated useful lives which range from one to five years and are recognized in cost of revenues in the consolidated statements of income and comprehensive income.

Software and maintenance contracts are recognized as prepaid expenses and other assets or within other long-term assets depending on their remaining useful lives.

Goodwill and Other Intangible Assets

Goodwill represents the excess of the purchase price and related costs over the value assigned to net assets acquired. Goodwill is not amortized, but is tested for impairment at least annually, or more often if events or circumstances indicate there may be impairment.

For 2016, the Company used a "qualitative assessment" option or "step zero" for the goodwill impairment test for all of its reporting units. With this process, the Company first assesses whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount. If the answer is no, then the fair value of the reporting unit does not need to be measured, and step one and step two, as explained below, are bypassed. In assessing the fair value of a reporting unit, which is based on the nature of the business and reporting unit's current and expected financial performance, the Company uses a combination of factors such as industry and market conditions, overall financial performance and the entity and reporting unit specific events.

In the past, the goodwill impairment test used was a two-step process at each reporting unit level. The first step used to identify potential impairment, compares the fair value of a reporting unit with its carrying amount, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is not considered impaired and the second step of the impairment test is not necessary. If the carrying amount of the reporting unit exceeds the fair value, there is an indication of potential impairment and the second step of the goodwill impairment analysis is required. The second step consists of comparing the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill.

For the years ended December 31, 2016, 2015 and 2014, no impairment losses associated with goodwill were recognized.

Other identifiable intangible assets with a definitive useful life are amortized using the straight-line method or an accelerated method. These intangibles are evaluated periodically for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

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Other identifiable intangible assets with a definitive useful life include a customer relationship, trademark, software packages and a non-compete agreement acquired during September 2010 when Apollo acquired a 51% indirect ownership interest in EVERTEC as part of a merger (the “Merger”); a customer relationship asset acquired in 2015 from a local bank in Puerto Rico, and customer relationship assets acquired as part of business combination transactions in 2016.

The customer relationship assets were valued using the excess earnings method under the income approach. Trademark assets were valued using the relief-from-royalty method under the income approach. Software packages, which include capitalized software development costs, were recorded at cost. The non-compete agreement was valued based on the estimated impact that theoretical competition would have on revenues and expenses.

Derivative Instruments and Hedging Activities

The Company uses derivative financial instruments to enhance its ability to manage its exposure to certain financial and market risks, primarily those related to changes in interest rates. On the date the derivative instrument contract is entered into, the Company may designate the derivative as (1) a hedge of the fair value of a recognized asset or liability or an unrecognized firm commitment (“fair value” hedge), (2) a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (“cash flow” hedge), or (3) as a “standalone” derivative instrument, including economic hedges that the Company has not formally documented as a fair value or cash flow hedge. Changes in the fair value of a derivative that qualifies for cash flow hedge accounting are recognized in Other Comprehensive Income (Loss). Amounts accumulated in other comprehensive income (loss) are reclassified to earnings when the related cash outflow affects earnings. Changes in the fair value of a derivative instrument that is highly effective and that is designated and qualifies as a fair value hedge, along with changes in the fair value of the hedged asset or liability that is attributable to the hedged risk (including gains or losses on firm commitments), are recorded in current-period earnings. Similarly, the changes in the fair value of stand-alone derivative instruments or derivatives not qualifying or designated for hedge accounting are reported in current-period earnings. The Company recognizes all derivative financial instruments in the Consolidated Balance Sheets as assets or liabilities at fair value. The Company does not enter into derivative financial instruments for speculative purposes.

Income Tax

Income taxes are accounted for under the asset and liability method. A temporary difference refers to a difference between the tax basis of an asset or liability, determined based on recognition and measurement requirements for tax positions, and its reported amount in the financial statements that will result in taxable or deductible amounts in future years when the reported amount of the asset or liability is recovered or settled, respectively. Deferred tax assets and liabilities represent the future effects on income taxes that result from temporary differences and carryforwards that exist at the end of a period. Deferred tax assets and liabilities are measured using enacted tax rates and provisions of the enacted tax law and are not discounted to reflect the time-value of money. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the consolidated statements of income and comprehensive income in the period that includes the enactment date. A deferred tax valuation allowance is established if it is considered more likely than not that all or a portion of the deferred tax asset will not be realized.

The Company recognizes the benefit of uncertain tax positions only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement or disposition of the underlying issue with the taxing authority. Accordingly, the amount of benefit recognized in the consolidated

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financial statements may differ from the amount taken or expected to be taken in the tax return resulting in unrecognized tax benefits (“UTBs”). The Company recognizes the interest and penalties associated with UTBs as part of the provision for income taxes on its consolidated statements of income and comprehensive income. Accrued interest and penalties are included on the related tax liability line in the consolidated balance sheets.

All companies within EVERTEC are legal entities which file separate income tax returns.

Cash

Cash includes cash on hand and in banks.

Restricted Cash

Restricted cash represents cash received on deposits from participating institutions of the ATH network that has been segregated for the development of the ATH brand and cash maintained as collateral for a credit facility with Popular. Also, restricted cash includes certain cash collected from the Ticketpop business and a reserve account for payment and transaction processing services to merchants. The restrictions of these accounts are based on contractual provisions entered into with third parties. This cash is maintained in separate accounts at a financial institution in Puerto Rico.

Allowance for Doubtful Accounts

An allowance for doubtful accounts is provided for based on the estimated uncollectible amounts of the related receivables. The estimate is primarily based on a review of the current status of specific accounts receivable. Receivables are considered past due if full payment is not received by the contractual date. Past due accounts are generally written off against the allowance for doubtful accounts only after all collection attempts have been exhausted.

Foreign Currency Translation

Assets and liabilities denominated in foreign currencies are translated to U.S. dollars using prevailing rates of exchange at the end of the period. Revenues, expenses, gains and losses are translated using weighted average rates for the period. The resulting foreign currency translation adjustment from operations for which the functional currency is other than the U.S. dollar is reported in accumulated other comprehensive loss. Gains and losses on transactions denominated in currencies other than the functional currencies are included in determining net income for the period in which exchange rates change.

Share-based Compensation

The Company estimates the fair value of stock-based awards, on a contemporaneous basis, at the date they are granted using the Black-Scholes-Merton option pricing model for Tranche A options and the Monte Carlo simulation analysis for Tranche B and Tranche C options and market based restricted stock units (“RSUs”) using the following assumptions: (1) stock price; (2) risk-free rate; (3) expected volatility; (4) expected annual dividend yield and (5) expected term. The risk-free rate is based on the U.S. Constant Maturities Treasury Interest Rate as of the grant date or the yield of a 2-year or 3-year Treasury bond, as applicable. The expected volatility is based on a combination of historical volatility and implied volatility from publicly traded companies in the Company’s industry. The expected annual dividend yield is based on management’s expectations of future dividends as of the grant date and, in certain cases, assumes that those dividends will be reinvested over the performance period. The expected term for stock options granted under the 2010 Plan was based on the vesting time of the options. For the stock options granted under the 2013 Plan, the simplified method was used to estimate the expected term,

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given that the Company did not have appropriate exercise data on which to base the estimate nor is exercise data relating to employees of comparable companies easily obtainable. Performance and time based RSUs and restricted stock are valued based on the market price of the Company's stock at the grant date.

Upon option exercise or restricted stock or RSUs release, participants may elect to "net share settle". Rather than requiring the participant to deliver cash to satisfy the exercise price, for options exercise, and statutory minimum tax withholdings, the Company withholds a sufficient number of shares to cover these amounts and delivers the net shares to the participant. The Company recognizes the associated tax withholding obligation as a reduction of additional paid-in capital.

As compensation expense is recognized, a deferred tax asset is established. At the time stock options are exercised, restricted stock or RSUs are released, a current tax deduction arises based on the value at the time of exercise or release. This deduction may exceed the associated deferred tax asset, resulting in a "windfall tax benefit". The windfall is recognized in the consolidated balance sheets as an increase to additional paid-in capital, and is included in the consolidated statements of cash flows as a financing inflow.

In determining the amount of cash tax savings realized from the excess share-based compensation deductions, the Company follows the tax law ordering approach. Under this approach, the utilization of excess tax deductions associated with share-based awards is dictated by provision in the tax law that identify the sequence in which such benefits are utilized for tax purposes.

Net Income per Common Share

Basic net income per common share is determined by dividing net income by the weighted-average number of common shares outstanding during the period.

Diluted net income per common share assumes the issuance of all potentially dilutive share equivalents using the treasury stock method. For stock options and RSUs it is assumed that the proceeds will be used to buy back shares. For stock options, such proceeds equal the average unrecognized compensation plus exercise price and windfall tax benefits. For unvested restricted share units, the proceeds equal the average unrecognized compensation plus windfall tax benefits.

Note 2—Recent Accounting Pronouncements

Recently adopted accounting pronouncements

In April, 2015, the Financial Accounting Standards Board ("FASB") issued updated guidance for accounting for fees paid in a cloud computing arrangement. The amendments in this Update provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The guidance will not change GAAP for a customer's accounting for service contracts. For public companies, the amendments in this Update were effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. The Company adopted this guidance on January 1, 2016. Its adoption did not have a material impact on our results from operations or financial position.

In April 2015, the FASB issued guidance requiring that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct reduction of the carrying amount of the debt liability, consistent with debt discounts. This guidance was effective for fiscal years beginning after December 15, 2015 and interim

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periods within those fiscal years. The Company adopted the guidance on January 1, 2016 and applied the standard retrospectively. The balance sheet presented has been adjusted to reflect the period specific effects of the adoption of the guidance. Specifically, debt issue costs of \$6.0 million and \$6.4 million for March 31, 2016, the adoption date, and December 31, 2015, respectively, were reclassified from other long-term assets to long-term debt within our unaudited Consolidated Condensed Balance Sheets.

In September 2015, the FASB issued updated guidance for Business Combinations and eliminated the requirement to retrospectively adjust the financial statements for measurement-period adjustments that occur in periods after a business combination is consummated. This guidance was effective for annual periods and interim periods within that period beginning after December 15, 2015. The Company adopted this guidance on January 1, 2016 with no impact.

In November 2015, the FASB issued updated guidance to simplify the classification of deferred income taxes. The amendments in this Update require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this Update apply to all entities that present a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this Update. The amendments in this Update are effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Earlier application is permitted for all entities as of the beginning of an interim or annual reporting period. The amendments in this Update may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. If an entity applies the guidance prospectively, the entity should disclose in the first interim and first annual period of change, the nature of and reason for the change in accounting principle and a statement that prior periods were not retrospectively adjusted. If an entity applies the guidance retrospectively, the entity should disclose in the first interim and first annual period of change the nature of and reason for the change in accounting principle and quantitative information about the effects of the accounting change on prior periods. The Company adopted this guidance on its balance sheet at June 30, 2016. The Company applied this guidance prospectively and the guidance was not retrospectively adjusted on the December 31, 2015 balance sheets. This guidance was adopted to simplify the presentation of deferred tax assets and liabilities.

Recently issued accounting pronouncements

The FASB has issued the following accounting pronouncements and guidance relevant to the Company's operations:

In February 2016, the FASB issued updated guidance for financial reporting about leasing transactions. The amendments in this Update require a lessee to recognize assets and liabilities for leases with lease terms of more than 12 months. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. In addition, the Update requires that both financing and operating leases be recognized on the balance sheet. The guidance also requires disclosures to help investors and other financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. These disclosures include qualitative and quantitative requirements, providing additional information about the amounts recorded in the financial statements. The amendments in this Update are effective for public companies for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements.

In March 2016, the FASB issued updated guidance for the effect of derivative contract novations on existing hedge accounting relationships. This Update clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require designation of that

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hedging relationship provided that all other hedge accounting criteria (including those in paragraphs 815-20-35-14 through 35-18) continue to be met. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. The Company expects to adopt this guidance with no impact on the consolidated financial statements.

In March 2016, the FASB issued updated guidance to simplify the transition to the equity method of accounting. The amendments in this Update affect all entities that have an investment that becomes qualified for the equity method of accounting as it eliminates the requirement that an investor adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. The amendments in this Update are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Earlier application is permitted. The Company expects to adopt this guidance if and when an investment becomes qualified for the equity method of accounting.

In March 2016, the FASB issued updated guidance for revenue from contracts with customers' principal versus agent considerations (reporting gross versus net). The amendments clarify the implementation guidance on principal versus agent considerations and are intended to improve the operability and understandability of the implementation guidance. The amendments in this Update affect the guidance in Accounting Standards Update 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements of Update 2014-09. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements.

In March 2016, the FASB issued updated guidance for accounting for employee share based payments. The areas for simplification in this Update involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. For public business entities, the amendments in this Update are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted for any entity in any interim or annual period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements.

In June 2016, the FASB issued updated guidance for the measurement of credit losses on financial instruments. The amendments in this Update require a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset or assets to present the net carrying value at the amount expected to be collected on the financial asset. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectibility of the reported amount. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. The amendments in this Update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. All entities may adopt the amendments in this Update earlier

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as of the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. An entity will apply the amendments in this Update through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements, if any.

In August 2016, the FASB issued updated guidance for the classification of certain cash receipts and cash payments on the statement of cash flows. The amendments in this update provide specific guidance for the classification of eight issues: debt prepayment or extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of an insurance claim; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and applications of the predominance principle. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. The amendments in this Update should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements, if any.

In October 2016, the FASB issued updated guidance for tax treatment of intra-entity transfers of assets other than inventory. Current GAAP prohibits the recognition of current and deferred income taxes for an intra-entity asset transfer until the asset has been sold to an outside party. The Board decided that an entity should recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. Consequently, the amendments in this Update eliminate the exception for an intra-entity transfer of an asset other than inventory. The amendments in this Update do not include new disclosure requirements; however, existing disclosure requirements might be applicable when accounting for the current and deferred income taxes for an intra-entity transfer of an asset other than inventory. For public business entities, the amendments in this Update are effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within those annual reporting periods. Early adoption is permitted for all entities as of the beginning of an annual reporting period for which financial statements (interim or annual) have not been issued or made available for issuance. The amendments in this Update should be applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements.

In October 2016, the FASB issued updated guidance for the consolidation of variable interest entities (“VIEs”) for which interests are held through related parties that are under common control. The amendments in this Update affect reporting entities that are required to evaluate whether they should consolidate a VIE within the Variable Interest Entities Subsections of Subtopic 810-10, Consolidation—Overall, in certain situations involving entities under common control. Specifically, the amendments change the evaluation of whether a reporting entity is the primary beneficiary of a VIE by changing how a reporting entity that is a single decision maker of a VIE treats indirect interests in the entity held through related parties that are under common control with the reporting entity. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period,

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any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. The Company is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements, if any.

In November 2016, the FASB issued guidance regarding the classification of transactions involving restricted cash on the statement of cash flows. The amendments in this Update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. The amendments in this Update should be applied using a retrospective transition method to each period presented. The Company will adopt this guidance on its consolidated statement of cash flows.

In January 2017, the FASB issued guidance clarifying the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The definition of a business affects many areas of accounting including acquisitions, disposals, goodwill, and consolidation. The amendments in this Update provide a screen to determine when a set is not a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This screen reduces the number of transactions that need to be further evaluated. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The amendments in this Update should be applied prospectively on or after the effective date. Early application of the amendments in this Update is allowed in specific circumstances. The Company will adopt this guidance on future acquisitions.

In January 2017, the FASB issued updated guidance to simplify the test for goodwill impairment. The amendments in this Update modify the concept of impairment from the condition that exists when the carrying amount of goodwill exceeds its implied fair value to the condition that exists when the carrying amount of a reporting unit exceeds its fair value. An entity no longer will determine goodwill impairment by calculating the implied fair value of goodwill by assigning the fair value of a reporting unit to all of its assets and liabilities as if that reporting unit had been acquired in a business combination. Because these amendments eliminate Step 2 from the goodwill impairment test, they should reduce the cost and complexity of evaluating goodwill for impairment. The amendments in this Update are effective for annual and interim goodwill impairment tests performed in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company is evaluating the impact of the adoption of this guidance on future goodwill impairment tests.

Accounting pronouncements issued prior to 2016 and not yet adopted

During 2014, the FASB issued new guidance for revenue from contracts with customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers and also includes changes in the accounting for customer contract acquisition costs and fulfillment costs. During 2016, the FASB issued several additional updates that amended the proposed guidance. These new standards will replace most existing revenue recognition guidance in U.S. GAAP, and are effective for public reporting companies for interim and annual periods beginning after December 15, 2017. The standards permit two methods of adoption: retrospectively to each prior reporting period presented (retrospective method),

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or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the cumulative catch-up transition method). The effective date for the Company is January 1, 2018. Management has not yet determined what transition method will be used.

Management is currently in the process of evaluating the potential impact this new guidance will have on the Company's financial statements. Management has not completed this evaluation and therefore, cannot conclude whether the guidance will have a significant impact on the financial statements at this time. However, based on preliminary work completed at this time, Management is considering the implications that the new standard may have in the following areas:

- Under the new standards, certain implementation costs and other fulfillment costs, such as direct labor for contract set-up activities, that are expensed as incurred under current policies, will be capitalized and amortized over the contract term and anticipated renewal periods.
- The period of amortization of contract acquisition costs (e.g., sales commissions) may change. Under current policies, sales commissions are expensed over the initial term of a contract. Under the new standards, these are required to be amortized over the initial contract term plus any anticipated renewal periods if there is no commensurate commission paid for the renewal periods.
- Under current policies, upfront activities (such as setup activities) are not generally analyzed to determine whether they have standalone value because the contingent revenue cap under the existing revenue guidance would prohibit allocation of hosting revenue to that upfront activity. Under the new standards, the contingent revenue cap no longer exists, so certain upfront activities included in the implementation process will need to be evaluated to determine whether they qualify as separate units of accounting. If they are separate units of accounting, then revenue would be allocated to the upfront activity, recognized as those activities are performed, rather than over the hosting period.
- Where the Company charges upfront fees for implementation or set-up activities, including fees charged in pre-production periods, the period over which these fees will be recognized may in some cases be shorter than our current practice.
- For certain software license arrangements, the Company currently uses a ratable, or over time, revenue recognition method for software licensing arrangements where vendor specific objective evidence (VSOE) of the maintenance portion of the arrangement does not exist. Under the new standards, Management expects the timing of revenue recognition to be accelerated because Management anticipates that the license revenue portion will be recognized at a point in time upon software license delivery.

At this time, Management is not able to reasonably estimate the impact that adoption is expected to have.

The Company's implementation process is ongoing. Significant activities that are in process are the calculation of the transition adjustment, drafting and approval of new accounting policies, and design and implementation of new processes and systems to accommodate the new policies and to compile the information for the enhanced disclosures under the new standards.

Note 3—Cash

At December 31, 2016 and 2015, the Company's cash amounted to \$51.9 million and \$28.7 million, respectively, which is mostly deposited in interest bearing deposit accounts within financial institutions. As of December 31, 2016 and 2015, total cash from subsidiaries located outside of Puerto Rico amounted to \$35.5 million and \$16.4 million, respectively. Cash deposited in an affiliate financial institution amounted to \$7.8 million and \$12.1 million as of December 31, 2016 and 2015, respectively.

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Note 4—Accounts Receivable, Net

Accounts receivable, net consisted of the following:

	December 31,	
	2016	2015
<i>(Dollar amounts in thousands)</i>		
Trade	\$52,663	\$52,652
Due from affiliates, net	20,971	16,886
Settlement assets	5,938	6,304
Other	144	123
Less: allowance for doubtful accounts	(1,913)	(2,250)
Accounts receivable, net	<u>\$77,803</u>	<u>\$73,715</u>

At December 31, 2016 and 2015, the Company had receivables from the government of Puerto Rico amounting to \$18.0 million and \$18.4 million, respectively, included as part of Trade receivables.

The Company records settlement assets that result from timing differences in the Company's settlement processes with merchants, financial institutions, and credit card associations related to merchant and card transaction processing. The amounts are generally collected or paid the following business day.

Note 5—Prepaid Expenses and Other Assets

Prepaid expenses and other assets consisted of the following:

	December 31,	
	2016	2015
<i>(Dollar amounts in thousands)</i>		
Software licenses and maintenance contracts	\$ 8,302	\$ 6,526
Deferred project costs	3,113	4,067
Guarantee deposits	3,396	2,404
Insurance	1,272	1,313
Prepaid income taxes	1,362	1,259
Taxes other than income	1,358	1,042
Postage	296	751
Other	1,331	1,396
Prepaid expenses and other assets	<u>\$20,430</u>	<u>\$18,758</u>

Note 6—Investment in Equity Investee

Consorcio de Tarjetas Dominicanas, S.A. ("CONTADO") is the largest merchant acquirer and ATM network in the Dominican Republic. The Company uses the equity method of accounting to account for its equity interest in CONTADO. As a result of the acquisition in 2011 of CONTADO's 19.99% equity interest, the Company calculated an excess cost of the investment in CONTADO over the amount of underlying equity in net assets of approximately \$9.0 million, which was mainly attributed to customer relationships, trademark and goodwill intangibles. The Company's excess basis allocated to amortizable assets is recognized on a straight-line basis over the lives of the appropriate intangibles. Amortization expense for each of the years ended December 31, 2016, 2015 and 2014 amounted to approximately \$0.3 million, and was recorded within earnings (losses) of equity method investment in the consolidated statements of income and comprehensive income. The Company recognized a loss of \$0.1 million for December 31, 2016 and earnings of \$0.1 million and \$1.1 million as equity in CONTADO's net income, net of amortization, in the consolidated statements of income and comprehensive

EVERTEC, Inc. Notes to Consolidated Financial Statements

income for the years ended 2015 and 2014, respectively. For the year ended December 31, 2014, the Company received \$0.3 million in dividends from CONTADO. No dividends were received during 2015 or 2016.

CONTADO fiscal year ends December 31 and is reported in the consolidated statements of income and comprehensive income for the period subsequent to the acquisition date on a one month lag. No significant events occurred in CONTADO's operations subsequent to November 30, 2016 that would have materially affected the Company's reported results.

Note 7—Property and Equipment, Net

Property and equipment, net consisted of the following:

<i>(Dollar amounts in thousands)</i>	Useful life in years	December 31,	
		2016	2015
Buildings	30	\$ 1,559	\$ 1,606
Data processing equipment	3 - 5	105,052	94,523
Furniture and equipment	3 - 20	7,311	8,170
Leasehold improvements	5 - 10	3,057	3,649
		116,979	107,948
Less—accumulated depreciation and amortization		(79,431)	(75,244)
Depreciable assets, net		37,548	32,704
Land		1,382	1,424
Property and equipment, net		<u>\$ 38,930</u>	<u>\$ 34,128</u>

Depreciation and amortization expense related to property and equipment was \$14.2 million, \$15.1 million and \$15.5 million for the years ended December 31, 2016, 2015 and 2014, respectively.

Note 8—Goodwill

The changes in the carrying amount of goodwill, allocated by reportable segments, were as follows (See Note 22):

<i>(Dollar amounts in thousands)</i>	Merchant acquiring, net	Payment processing	Business solutions	Total
Balance at December 31, 2014	\$138,121	\$184,228	\$46,488	\$368,837
Foreign currency translation adjustments	—	(732)	28	(704)
Balance at December 31, 2015	138,121	183,496	46,516	368,133
Goodwill attributable to acquisition	—	4,991	—	4,991
Foreign currency translation adjustments	—	(1,799)	(339)	(2,138)
Balance at December 31, 2016	<u>\$138,121</u>	<u>\$186,688</u>	<u>\$46,177</u>	<u>\$370,986</u>

Goodwill is tested for impairment on an annual basis, or more often if events or circumstances indicate there may be impairment. For 2016, the Company used the qualitative assessment option or step zero process. Using this process, the Company first assesses whether it is “more likely than not” that the fair value of a reporting unit is less than its carrying amount. For 2015, the Company used a two-step process at each reporting unit level. The first step (“Step 1”) compares the estimated fair value of the reporting units to their carrying values, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is not considered impaired and the second step of the impairment test is unnecessary. If needed, the second step

EVERTEC, Inc. Notes to Consolidated Financial Statements

(“Step 2”) consists of comparing the implied fair value of the reporting units with the carrying amount of that goodwill.

The Company conducted a qualitative assessment of each reporting unit’s fair value, or step zero process, as of August 31, 2016. As part of the Company’s qualitative assessment, EVERTEC considered the results for the Company’s 2015 impairment test (which indicated that the fair value of each reporting unit was in excess of its carrying amount by 120.9%—145.5%) as well as current market conditions and changes in the carrying amount of the Company’s reporting units that occurred subsequent to the 2015 impairment test. Based on the results of this qualitative assessment, EVERTEC believes the fair value of goodwill for each of the Company’s reporting units continues to exceed their respective carrying amounts and concluded that it was not necessary to conduct the two-step goodwill impairment test. Accordingly, no impairment losses for the period were recognized.

Note 9—Other Intangible Assets, Net

The carrying amount of other intangible assets consisted of the following:

(Dollar amounts in thousands)

	Useful life in years	December 31, 2016		
		Gross amount	Accumulated amortization	Net carrying amount
Customer relationships	8 - 14	\$334,455	\$(141,829)	\$192,626
Trademark	10 - 15	39,950	(21,650)	18,300
Software packages	3 - 10	176,267	(121,055)	55,212
Non-compete agreement	15	56,539	(23,558)	32,981
Other intangible assets, net		<u>\$607,211</u>	<u>\$(308,092)</u>	<u>\$299,119</u>

(Dollar amounts in thousands)

	Useful life in years	December 31, 2015		
		Gross amount	Accumulated amortization	Net carrying amount
Customer relationships	10 - 14	\$322,632	\$(117,963)	\$204,669
Trademark	10 - 15	39,950	(18,186)	21,764
Software packages	3 - 10	155,611	(106,735)	48,876
Non-compete agreement	15	56,539	(19,789)	36,750
Other intangible assets, net		<u>\$574,732</u>	<u>\$(262,673)</u>	<u>\$312,059</u>

The Company completed two acquisitions in 2016 that were not significant, individually or in the aggregate, a 65% equity interest in Processa, S.A.S, a Colombian payment processing company for \$6.4 million, including a customer relationship of \$3.1 million, and Accuprint, Inc, a data management and printing services company for \$9.7 million, including a customer relationship of \$9.1 million. In connection with the Accuprint, Inc purchase, the Company has recorded a contingent liability of \$1.1 million. The results of operations and financial position of these entities are included in the Consolidated Financial Statements from and after the date of acquisition. During 2015, the Company acquired a customer relationship amounting to \$10.0 million.

Amortization expense related to intangibles, including software packages, was \$45.4 million, \$49.9 million and \$50.5 million for the years ended December 31, 2016, 2015 and 2014, respectively. Amortization expense related to software packages was \$14.3 million, \$20.1 million and \$21.0 million for the years ended December 31, 2016, 2015 and 2014, respectively. During the year ended December 31, 2016, the Company recognized an impairment

EVERTEC, Inc. Notes to Consolidated Financial Statements

loss of \$2.3 million related to software. The estimated amortization expenses of balances outstanding at December 31, 2016 for the next five years are as follows:

<i>(Dollar amounts in thousands)</i>	
2017	\$43,723
2018	39,516
2019	36,247
2020	33,621
2021	32,465

Note 10—Other Long-Term Assets

As of December 31, 2016, other long-term assets included \$1.9 million related to deferred debt-issuance costs related to the revolving credit facility, \$2.3 million related to the long-term portion of certain software and maintenance contracts and \$1.1 million relating to the long-term portion of certain lease receivables.

As of December 31, 2015, other long-term assets included \$1.3 million related to deferred debt-issuance costs related to the revolving credit facility and \$1.7 million related to the long-term portion of certain software and maintenance contracts.

Note 11—Debt and Short-Term Borrowings

Total debt was as follows:

<i>(Dollar amounts in thousands)</i>		December 31,	
		2016	2015
Senior Secured Credit Facility (Term A) due on April 17, 2018 paying interest at a variable interest rate (London InterBank Offered Rate (“LIBOR”) plus applicable margin ⁽¹⁾⁽³⁾)	\$ —	\$260,324	
Senior Secured Credit Facility (2018 Term A) due on April 17, 2018 paying interest at a variable interest rate (London InterBank Offered Rate (“LIBOR”) plus applicable margin ⁽¹⁾⁽³⁾)	28,721	—	
Senior Secured Credit Facility (2020 Term A) due on January 17, 2020 paying interest at a variable interest rate (London InterBank Offered Rate (“LIBOR”) plus applicable margin ⁽³⁾⁽⁴⁾)	212,661	—	
Senior Secured Credit Facility (Term B) due on April 17, 2020 paying interest at a variable interest rate (LIBOR plus applicable margin ⁽²⁾⁽³⁾)	378,074	381,723	
Senior Secured Revolving Credit Facility ⁽⁶⁾	28,000	17,000	
Note Payable due on October 1, 2017 ⁽³⁾	1,524	2,967	
Note Payable due on July 31, 2017 ⁽³⁾	357	685	
Note Payable due on August 31, 2019 ⁽⁵⁾	890	—	
Note Payable due on April 30, 2021 ⁽³⁾	532	—	
Total debt	<u>\$650,759</u>	<u>\$662,699</u>	

⁽¹⁾ Applicable margin of 2.25% at December 31, 2016 and 2015.

⁽²⁾ Subject to a minimum rate (“LIBOR floor”) of 0.75% applicable margin of 2.50% at December 31, 2016 and 2015, respectively.

⁽³⁾ Net of unaccreted discount and unamortized debt issue costs, as applicable.

⁽⁴⁾ Applicable margin of 2.50% at December 31, 2016.

⁽⁵⁾ Fixed interest rate of 7.50%.

⁽⁶⁾ Applicable margin of 2.50% and 2.25% at December 31, 2016 and 2015, respectively.

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The following table presents contractual principal payments for the next five years:

<i>(Dollar amounts in thousands)</i>	
2017	\$ 50,162
2018	46,953
2019	24,924
2020	540,820
2021	45

Senior Secured Credit Facilities

On April 17, 2013, EVERTEC Group entered into a credit agreement (the “2013 Credit Agreement”) governing the senior secured credit facilities, consisting of a \$300.0 million term loan A facility (the “Term A Loan”), a \$400.0 million term loan B facility (the “Term B Loan”) and a \$100.0 million revolving credit facility.

Term A Loan

The Term A Loan requires principal payments on the last business day of each quarter equal to (a) 1.250% of the original principal amount commencing on September 30, 2013 through June 30, 2016; (b) 1.875% of the original principal amount from September 30, 2016 through June 30, 2017; (c) 2.50% of the original principal amount from September 30, 2017 through March 31, 2018; and (d) the remaining outstanding principal amount on the maturity of the Term A Loan on April 17, 2018. Interest is based on EVERTEC Group first lien secured net leverage ratio and payable at a rate equal to, at the Company’s option, either (a) LIBOR Rate plus an applicable margin ranging from 2.00% to 2.50%, or (b) Alternate Base Rate (“ABR”), as defined in the 2013 Credit Agreement, plus an applicable margin ranging from 1.00% to 1.50%. The Term A Loan has no LIBOR or Base Rate minimum or floor.

Term B Loan

The Term B Loan requires principal payments on the last business day of each quarter equal to 0.250% of the original principal amount commencing on September 30, 2013 and the remaining outstanding principal amount on the maturity of the Term B Loan on April 17, 2020. Interest is based on EVERTEC Group’s first lien secured net leverage ratio and payable at a rate equal to, at the Company’s option, either (a) LIBOR Rate plus an applicable margin ranging from 2.50% to 2.75%, or (b) Base Rate plus an applicable margin ranging from 1.50% to 1.75%. The LIBOR Rate and Base Rate are subject to floors of 0.75% and 1.75%, respectively.

Revolving Credit Facility

The revolving credit facility has an available balance up to \$100.0 million, with an interest rate on loans calculated the same as the applicable Term A Loan rate. The facility matures on April 17, 2018 and has a “commitment fee” payable one business day after the last business day of each quarter calculated based on the daily unused commitment during the preceding quarter. The commitment fee for the unused portion of this facility ranges from 0.125% to 0.375% and is based on EVERTEC Group’s first lien secured net leverage ratio.

All loans may be prepaid without premium or penalty.

The senior secured credit facilities contain various restrictive covenants. As a result of the Third Amendment (as defined below), the Term A Loan and the revolving credit facility (subject to certain exceptions) require the Company to maintain on a quarterly basis a specified maximum senior secured leverage ratio of up to 4.75 to 1.00 as defined in the 2013 Credit Agreement (total first lien secured debt to adjusted EBITDA) until

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September 30, 2018 and 4.25 to 1.00 for any fiscal quarter ending thereafter. In addition, substantially all of the Company's assets are pledged to secure the Company's obligations under the 2013 Credit agreement and, among other things, the 2013 Credit Agreement: (a) limits the Company's ability and the ability of the Company's subsidiaries to incur additional indebtedness, incur liens, pay dividends or make certain other restricted payments, as all net assets are restricted, and enter into certain transactions with affiliates; (b) restricts the Company's ability to enter into agreements that would restrict the ability of the Company's subsidiaries to pay dividends or make certain payments to EVERTEC; and (c) places restrictions on the Company's ability and the ability of the Company's subsidiaries to merge or consolidate with any other person or sell, assign, transfer, convey or otherwise dispose of all or substantially all of the Company's assets.

Amendments to the 2013 Credit Agreement

During the second quarter of 2016, EVERTEC Group, together with certain other direct and indirect subsidiaries of the Company, entered into a second amendment and waiver to the outstanding Credit Agreement (the "Second Amendment"). The Company paid each lender that consented to the amendment a fee equal to 0.50% of the aggregate principal amount of outstanding term loans and revolving commitments held by such lender. The credit amendment fees paid during the second quarter of 2016 amounted to \$3.6 million.

During the fourth quarter of 2016, EVERTEC Group, together with certain other direct and indirect subsidiaries of the Company, entered into a third amendment (the "Third Amendment") to the 2013 Credit Agreement. The Third Amendment extends the maturity of (a) approximately \$219 million of EVERTEC Group's existing approximately \$250 million of Term A loan facility to January 17, 2020 (the "2020 Term A loan") and (b) \$65 million of EVERTEC Group's existing \$100 million of revolving credit facility to January 17, 2020. The remaining approximately \$30 million of Term A loan (the "2018 Term A loan") and the \$35 million of revolving credit facility that were not extended will remain in place and mature as originally scheduled on April 17, 2018. The Term B loan facility will remain in place and mature as originally scheduled on April 17, 2020 (collectively, the "Senior Secured term loans").

Under the terms of the Third Amendment, the 2018 Term A Loan amortizes on a basis of 1.875% of the original principal amount beginning in the third quarter of 2016 and during each of the next three quarters, and 2.50% of the original principal amount during each of the final three quarters, with the balance payable on the final maturity date. The 2020 Term A Loan amortizes on a basis of 1.50% of the original principal amount beginning in the fourth quarter of 2016 and during each of the next five quarters, 1.875% of the original principal amount during each of the four subsequent quarters, and 2.50% of the original principal amount during each of the final three quarters, with the balance payable on the final maturity date.

The applicable margin under the 2013 Credit Agreement is based on, at EVERTEC Group's option, (i) with respect to any 2018 Term A Loan, 2.50% per annum in the case of any LIBOR Loan and 1.50% per annum in the case of any ABR Loan subject to reduction based on achievement of specific first lien secured leverage ratios, (ii) with respect to any 2020 Term A Loan, 2.50% per annum in the case of any LIBOR Loan and 1.50% per annum in the case of any ABR Loan, (iii) with respect to any Term B Loan, 2.75% per annum in the case of any LIBOR Loan and 1.75% per annum in the case of any ABR Loan subject to reduction based on achievement of specific first lien secured leverage ratios, and (iv) with respect to any Revolving Facility Loan, (A) 2.50% per annum in the case of any LIBOR Loan and (B) 1.50% per annum in the case of any ABR Loan.

The unpaid principal balance at December 31, 2016 of the 2018 Term A Loan, the 2020 Term A Loan and the Term B Loan was \$29.5 million, \$216.0 million and \$386.0 million, respectively. The additional borrowing capacity for the Revolving Facility loan at December 31, 2016 was \$72.0 million.

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Notes payable

In December 2014, June 2015, and May 2016, EVERTEC Group entered into non-interest bearing financing agreements amounting to \$4.6 million, \$1.1 million and \$0.7 million, respectively, and in October 2016 entered into an interest bearing agreement of \$1.1 million, to purchase software. As of December 31, 2016 and 2015, the outstanding principal balance of the notes payable was \$3.4 million and \$4.2 million, respectively. The current portion of these notes is recorded as part of accounts payable and the long-term portion is included in other long-term liabilities.

Interest Rate Swap

As of December 31, 2016 and 2015, the Company has the following interest rate swap agreement converting a portion of the interest rate exposure on the Company's Term B loan from variable to fixed:

<u>Effective date</u>	<u>Maturity Date</u>	<u>Notional Amount</u>	<u>Variable Rate</u>	<u>Fixed Rate</u>
January 2017	April 2020	\$200 million	1-month LIBOR	1.9225%

The Company has accounted for this transaction as a cash flow hedge. The fair value of the Company's derivative instruments is determined using standard valuation models. The significant inputs used in these models are readily available in public markets, or can be derived from observable market transactions, and therefore have been classified as Level 2. Inputs used in these standard valuation models for derivative instruments include the applicable forward rates and discount rates.

As of December 31, 2016 and 2015, the carrying amount of the derivative on the Company's balance sheets is as follows:

<i>(Dollar amounts in thousands)</i>	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Other long-term liabilities	\$1,964	\$515

The cash flow hedge is considered highly effective and no impact on earnings is expected due to hedge ineffectiveness.

Note 12—Financial Instruments and Fair Value Measurements

Recurring Fair Value Measurements

Fair value measurement provisions establish a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. These provisions describe three levels of input that may be used to measure fair value:

Level 1: Inputs are unadjusted, quoted prices for identical assets or liabilities in active markets at the measurement date.

Level 2: Inputs, other than quoted prices included in Level 1, which are observable for the asset or liability through corroboration with market data at the measurement date.

Level 3: Unobservable inputs that reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date.

The Company uses observable inputs when available. Fair value is based upon quoted market prices when available. If market prices are not available, the Company may employ models that mostly use market-based inputs including yield curves, interest rates, volatilities, and credit curves, among others. The Company limits

EVERTEC, Inc. Notes to Consolidated Financial Statements

valuation adjustments to those deemed necessary to ensure that the financial instrument's fair value adequately represents the price that would be received or paid in the marketplace. Valuation adjustments may include consideration of counterparty credit quality and liquidity as well as other criteria. The estimated fair value amounts are subjective in nature and may involve uncertainties and matters of significant judgment for certain financial instruments. Changes in the underlying assumptions used in estimating fair value could affect the results. The fair value measurement levels are not indicative of risk of investment.

The fair value of financial instruments is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value estimates are made at a specific point in time based on the type of financial instrument and relevant market information. Many of these estimates involve various assumptions and may vary significantly from amounts that could be realized in actual transactions. The following table summarizes fair value measurements by level at December 31, 2016 and 2015, for assets and liabilities measured at fair value on a recurring basis:

<i>(Dollar amounts in thousands)</i>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
December 31, 2016				
Financial liabilities:				
Interest rate swap	\$—	\$1,964	\$—	\$1,964
December 31, 2015				
Financial liabilities:				
Interest rate swap	—	515	—	515

Derivative Instruments

The fair value of the Company's derivative instrument is determined using a standard valuation model. The significant inputs used in these models are readily available in public markets, or can be derived from observable market transactions, and therefore have been classified as Level 2. Inputs used in these standard valuation models for derivative instruments include the applicable forward rates and discount rates. The discount rates are based on the historical LIBOR Swap rates.

The following table presents the carrying value, as applicable, and estimated fair values for financial instruments at December 31, 2016 and 2015:

<i>(Dollar amounts in thousands)</i>	<u>December 31,</u>			
	<u>2016</u>		<u>2015</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Financial liabilities:				
Interest rate swap	\$ 1,964	\$ 1,964	\$ 515	\$ 515
Senior secured Term A Loan	—	—	260,324	250,688
Senior secured Term B Loan	378,074	383,491	381,723	373,749
2018 Term A Loan	28,721	29,268	—	—
2020 Term A Loan	212,661	213,872	—	—

The fair value of the senior secured term loans at December 31, 2016 and 2015 was obtained using the prices provided by third party service providers. Their pricing is based on various inputs such as: market quotes, recent trading activity in a non-active market or imputed prices. Also, the pricing may include the use of an algorithm that could take into account movement in the general high yield market, among other variants.

The senior secured term loans, which are not measured at fair value in the balance sheets, if measured, would be categorized as Level 3 in the fair value hierarchy.

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There were no transfers in or out of Level 3 during the years ended December 31, 2016, 2015 and 2014.

Note 13—Other Long Term Liabilities

As of December 31, 2016, other long-term liabilities mainly consists of unrecognized tax benefit liabilities and the long-term portion of notes payables of \$14.4 million and derivative liability of \$2.0 million.

As of December 31, 2015, other long-term liabilities mainly consists of unrecognized tax benefit liabilities and the long-term portion of notes payables of \$11.6 million and derivative liability of \$0.5 million.

Note 14—Equity

The Company is authorized to issue up to 206,000,000 shares of common stock of \$0.01 par value. At December 31, 2016 and 2015, the Company had 72,635,032 and 74,988,210 shares outstanding, respectively. The Company is also authorized to issue 2,000,000 shares of \$0.01 par value preferred stock. As of December 31, 2016, no shares of preferred stock have been issued.

Stock Repurchase

In 2016, 2015 and 2014, the Company repurchased a total of 2.5 million, 3.0 million and 1.2 million shares, respectively, at a cost of \$39.9 million, \$54.9 million and \$26.2 million, respectively. The Company funded such repurchases with cash on hand and borrowings to the existing revolving credit facility. As of December 31, 2016, 2015 and 2014, the repurchased shares were permanently retired.

Dividends

EVERTEC pays a regular quarterly dividend on the Company's common stock, subject to the declaration thereof each quarter by the Company's Board of Directors. The Company's dividend activity in 2016 and 2015 was as follows:

<u>Declaration Date</u>	<u>Record Date</u>	<u>Payment Date</u>	<u>Dividend per share</u>
February 18, 2015	March 2, 2015	March 19, 2015	0.10
May 6, 2015	May 18, 2015	June 5, 2015	0.10
August 5, 2015	August 17, 2015	September 3, 2015	0.10
November 4, 2015	November 16, 2015	December 4, 2015	0.10
February 17, 2016	February 29, 2016	March 17, 2016	0.10
May 11, 2016	May 23, 2016	June 10, 2016	0.10
July 28, 2016	August 9, 2016	September 2, 2016	0.10
October 27, 2016	November 14, 2016	December 2, 2016	0.10

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Accumulated Other Comprehensive loss

The following tables provides a summary of the changes in the balances of accumulated other comprehensive loss for the years ended December 31, 2016 and 2015:

	<u>Foreign Currency Translation Adjustments</u>	<u>Cash Flow Hedge</u>	<u>Total</u>
Balance—December 31, 2014	\$ (6,522)	\$ —	\$ (6,522)
Additions:	<u>(545)</u>	<u>(515)</u>	<u>(1,060)</u>
Balance—December 31, 2015	(7,067)	(515)	(7,582)
Additions:	<u>(3,360)</u>	<u>(1,449)</u>	<u>(4,809)</u>
Balance—December 31, 2016	<u><u>\$(10,427)</u></u>	<u><u>\$(1,964)</u></u>	<u><u>\$(12,391)</u></u>

Note 15—Share-based Compensation

Equity Incentive Plans

On September 30, 2010, Holdings Board of Directors adopted the Carib Holdings, Inc. 2010 Equity Incentive Plan (the “2010 Plan”) to grant stock options, rights to purchase shares, restricted stock units and other stock-based rights to employees, directors, consultants and advisors. On April 17, 2012, in connection with the Company’s reorganization, EVERTEC, Inc. assumed the 2010 Plan and all of the outstanding equity awards issued thereunder or subject thereto. EVERTEC, Inc. reserved 5,843,208 shares of its common stock for issuance upon exercise and grants of stock options, restricted stock and other equity awards under the 2010 Plan.

In connection with the Company’s initial public offering, the Company adopted the EVERTEC, Inc. 2013 Equity Incentive Plan (the “2013 Plan” and, together with the 2010 Plan, the “Equity Incentive Plans”). Under the 2013 Plan, 5,956,882 shares of its common stock are reserved for issuance upon exercise and grants of stock options, restricted stocks and other equity awards. In connection with the adoption of the 2013 Plan, the 2010 Plan remains in effect. However, no new awards will be granted under the 2010 Plan. The Equity Incentive Plans have a contractual term of ten years.

Long-term Incentive Plan

In the first quarter of 2015, the Compensation Committee of the Board of Directors approved grants of restricted stock units (“RSUs”) to executives and certain employees pursuant to the 2015 Long-Term Incentive Program (“LTIP”) under the terms of our 2013 Equity Incentive Plan. Under the LTIP, the Company granted restricted stock units to eligible participants as time-based awards and/or performance-based awards.

In the first quarter of 2016, the Compensation Committee of the Board of Directors approved grants of RSUs to executives and certain employees pursuant to the 2016 Long-Term Incentive Program (“2016 LTIP”) under the terms of our 2013 Equity Incentive Plan. Under the 2016 LTIP, the Company granted restricted stock units to eligible participants as time-based awards and/or performance-based awards.

The vesting of the RSUs is dependent upon service, market, and/or performance conditions as defined in the grants. Employees that received time-based awards with service conditions are entitled to receive a specific number of shares of the Company’s common stock on the vesting date if the employee is providing services to the Company on the vesting date. Time-based awards vest over a period of three years in substantially equal installments commencing on the start of the fiscal year during which the RSUs were granted or on the grant date and ending on January 1st of each year for the 2015 LTIP and in mid-February of each year for the 2016 LTIP.

EVERTEC, Inc. Notes to Consolidated Financial Statements

Employees that received awards with market conditions are entitled to receive a specific number of shares of the Company's common stock on the vesting date if the Company's total shareholder return ("TSR") target relative to a specified group of industry peer companies is achieved. Employees that received awards with performance conditions are entitled to receive a specific number of shares of the Company's common stock on the vesting date if the Cumulative Annual Growth Rate ("CAGR") of Diluted EPS target is achieved. Performance and market-based awards vest at the end of the performance period which commenced on the start of the fiscal year during which the RSUs were granted and ends on January 1, 2018 for 2015 LTIP and February 2019 for 2016 LTIP. Awards are forfeited if the employee voluntarily ceases to be employed by the Company prior to vesting.

The following table summarizes the stock options activity for the years ended December 31, 2016, 2015 and 2014:

	<u>Shares</u>	<u>Weighted-average exercise prices</u>
Outstanding at December 31, 2013	1,285,536	\$ 4.77
Granted	100,000	24.01
Forfeitures	(31,164)	1.30
Exercised ⁽¹⁾	(945,040)	1.96
Repurchased	(93,332)	4.83
Outstanding at December 31, 2014	316,000	\$19.56
Expired	(50,000)	23.36
Forfeitures	(126,000)	18.81
Outstanding at December 31, 2015	140,000	\$18.88
Forfeitures	(33,333)	24.01
Exercised	(20,000)	6.04
Expired	(66,667)	24.01
Outstanding at December 31, 2016	<u>20,000</u>	<u>\$ 6.04</u>
Exercisable at December 31, 2016	<u>—</u>	<u>\$ —</u>

⁽¹⁾ As of December 31, 2016 and 2014, the total intrinsic value of options exercised amounted to \$0.2 million and \$19.3 million, respectively.

The following table presents information about fully vested stock options for the years ended December 31, 2016, 2015 and 2014:

	Years ended December 31,					
	2016		2015		2014	
	<u>Shares</u>	<u>Weighted average exercise price</u>	<u>Shares</u>	<u>Weighted average exercise price</u>	<u>Shares</u>	<u>Weighted average exercise price</u>
Vested stock options ⁽¹⁾⁽²⁾⁽³⁾	—	\$—	33,333	\$24.01	766,995	\$3.75

⁽¹⁾ At December 31, 2015, there is no intrinsic value for vested stock options as the options are out-of-the-money. For December 31, 2014, the aggregate intrinsic value amounted to \$14.0 million.

⁽²⁾ The weighted average contractual term of fully vested options is 8.16 years and 6.06 years as of December 31, 2015 and 2014, respectively.

⁽³⁾ The fair value of vested stock options at December 31, 2015 and 2014 amounted to \$1.4 million and \$17.0 million, respectively.

EVERTEC, Inc. Notes to Consolidated Financial Statements

Management uses the fair value method of recording stock-based compensation as described in the guidance for stock compensation in ASC topic 718. No stock options were granted in 2016 and 2015. The fair value of stock options granted during 2014, was estimated using the Black-Scholes-Merton (“BSM”) option pricing model, with the following assumptions:

	<u>Year ended December 31, 2014</u>
	<u>Stock options granted under the 2013 Plan</u>
Stock Price	\$24.01 per share
Risk-free rate	1.80%
Expected volatility	36.98%
Expected annual dividend yield	1.63%
Expected term	6 years

The risk-free rate is based on the U.S. Constant Maturities Treasury Interest Rate as of the grant date. The expected volatility is based on a combination of historical volatility and implied volatility from public trade companies in the Company’s industry. The expected annual dividend yield is based on management’s expectations of future dividends as of the grant date. The expected term for stock options granted under the 2010 Plan was based on the vesting time of the options. For the stock options granted under the 2013 Plan, the simplified method was used to estimate the expected term.

The following table summarizes the nonvested restricted shares and RSUs activity for the years ended December 31, 2016, 2015 and 2014:

<u>Nonvested restricted shares and RSUs</u>	<u>Shares</u>	<u>Weighted-average grant date fair value</u>
Nonvested at December 31, 2013	9,133	\$26.64
Granted	23,252	22.04
Vested	(9,133)	24.64
Nonvested at December 31, 2014	23,252	\$22.04
Granted	596,238	22.24
Vested	(94,550)	21.33
Forfeited	(33,214)	23.61
Nonvested at December 31, 2015	491,726	\$22.32
Granted	907,320	12.02
Vested	(154,820)	20.97
Forfeited	(31,862)	18.61
Nonvested at December 31, 2016	<u>1,212,364</u>	<u>\$14.88</u>

Share-based compensation recognized was as follows:

	<u>Years ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
<i>(Dollar amounts in thousands)</i>			
Share-based compensation recognized, net Stock options	\$ 60	\$ 192	\$4,305
Restricted shares and RSUs	6,355	5,010	282

Pursuant to the terms of the 2010 Plan, Tranche A stock options will generally vest in five equal installments, except for some grants as specified in the stock agreement, Tranche B options granted to employees and certain

EVERTEC, Inc. Notes to Consolidated Financial Statements

directors would vest at such time as the Investor Internal Rate of Return (“IRR”) equals or exceeds 25%, except for one grant that vests upon a 20% IRR, based on cash proceeds received by Apollo Investment Fund VII, L.P. (the “Investor”), and Tranche C options would vest at such time as the IRR equals or exceeds 30% based on cash proceeds received by the Investor.

The unrecognized share-based compensation expense related to the stock options was not significant at December 31, 2016.

At December 31, 2016, the maximum unrecognized cost for restricted stock and RSUs was \$11.3 million. The cost is expected to be recognized over a weighted average period of 1.79 years.

Note 16—Employee Benefit Plan

EVERTEC, Inc. Puerto Rico Savings and Investment plan (“the EVERTEC Savings Plan”) was established, as a defined contribution savings plan qualified under section 1165(e) of the Puerto Rico Internal Revenue Code. Investments in the plan are participant directed, and employer matching contributions are determined based on specific provisions of the EVERTEC Savings Plan. Employees are fully vested in the employer’s contributions after five years of service. For the years ended December 31, 2016, 2015 and 2014, the costs incurred under the plan amounted to approximately \$0.7 million, \$0.8 million and \$0.6 million, respectively.

Note 17—Total Other Income, Net

For the year ended December 31, 2016, other income (expenses) is primarily comprised of \$1.9 million in foreign currency transaction gains and \$1.5 million loss on the extinguishment of debt (Note 11).

For the year ended December 31, 2015, other income (expenses) is primarily comprised of \$1.2 million in foreign currency transaction gains, \$0.2 million in gains related to adjustments made to software indemnification assets during the year, \$0.4 million in sales rebates granted to EVERTEC and a \$0.2 million gain related to certain refurbished POS machines.

For the year ended December 31, 2014, other income (expenses) is primarily comprised of \$2.6 million in foreign currency transaction gains and a \$0.4 million in expenses related to adjustments made to software indemnification assets as a result of certain maintenance contract cancellations during the year.

Note 18—Income Tax

On April 17, 2012, EVERTEC Group and Holdings were converted from a Puerto Rico corporation into Puerto Rico limited liability companies to benefit from changes to the Puerto Rico Income Tax Code allowing limited liability companies to be treated as partnerships that are pass-through entities for Puerto Rico tax purposes. As a result of these conversions and subsequent elections to be treated as partnerships, EVERTEC Group’s and Holding’s taxable income flows through to EVERTEC, Inc.

EVERTEC Group, Holdings and EVERTEC, Inc. entered into a Tax Payment Agreement pursuant to which EVERTEC Group is obligated to make certain payments to Holdings or EVERTEC, Inc. for taxable periods or portions thereof occurring on or after April 17, 2012 (the “Effective Date”). Under the Tax Payment Agreement, EVERTEC Group will make payments with respect to any and all taxes (including estimated taxes) imposed under the laws of Puerto Rico, the United States of America and any other jurisdiction or any political (including municipal) subdivision or authority or agency in Puerto Rico, the United States of America or such other jurisdiction, that would have been imposed on EVERTEC Group if EVERTEC Group had been a corporation for tax purposes of that jurisdiction, together with all interest and penalties with respect thereto (“Taxes”), reduced

EVERTEC, Inc. Notes to Consolidated Financial Statements

by taking into account any applicable net operating losses or other tax attributes of Holdings or EVERTEC, Inc. that reduce Holdings' or EVERTEC, Inc.'s taxes in such period. The Tax Payment Agreement provides that the payments thereunder shall not exceed the net amount of Taxes that Holdings and EVERTEC, Inc. actually owe to the appropriate taxing authority for a taxable period. Further, the Tax Payment Agreement provides that if Holdings or EVERTEC, Inc. receives a tax refund attributable to any taxable period or portion thereof occurring on or after the Effective Date, EVERTEC, Inc. shall be required to recalculate the payment for such period required to be made by EVERTEC Group to Holdings or EVERTEC, Inc. If the payment, as recalculated, is less than the amount of the payment EVERTEC Group already made to Holdings or EVERTEC, Inc. in respect of such period, Holdings or EVERTEC, Inc. shall promptly make a payment to EVERTEC Group in the amount of such difference.

The components of income tax expense (benefit) consisted of the following:

	<u>Years ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
<i>(Dollar amounts in thousands)</i>			
Current tax provision (benefit)	\$12,865	\$ (245)	\$12,602
Deferred tax benefit	(4,594)	(3,090)	(3,701)
Income tax expense (benefit)	<u>\$ 8,271</u>	<u>\$(3,335)</u>	<u>\$ 8,901</u>

The Company conducts operations in Puerto Rico and certain countries throughout the Caribbean and Latin America. As a result, the income tax expense (benefit) includes the effect of taxes paid to the Puerto Rico government as well as foreign jurisdictions. The following table presents the segregation of income tax expense (benefit) based on location of operations:

	<u>Years ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
<i>(Dollar amounts in thousands)</i>			
Income before income tax provision (benefit)			
Puerto Rico	\$70,899	\$73,327	\$61,759
United States	2,670	1,879	2,131
Foreign countries	9,828	6,836	11,168
Total income before income tax provision (benefit)	<u>\$83,397</u>	<u>\$82,042</u>	<u>\$75,058</u>
Current tax provision (benefit)			
Puerto Rico	7,072	(3,500)	8,090
United States	567	413	(517)
Foreign countries	5,226	2,842	5,029
Total current tax provision (benefit)	<u>\$12,865</u>	<u>\$ (245)</u>	<u>\$12,602</u>
Deferred tax benefit			
Puerto Rico	(2,874)	(2,169)	(1,933)
United States	(259)	(114)	(124)
Foreign countries	(1,461)	(807)	(1,644)
Total deferred tax benefit	<u>\$(4,594)</u>	<u>\$(3,090)</u>	<u>\$(3,701)</u>

Taxes payable to foreign countries by EVERTEC's subsidiaries will be paid by such subsidiary and the corresponding liability and expense will be presented in EVERTEC's consolidated financial statements.

On June 30, 2013, the Governor of Puerto Rico signed into law Act 40, effective as of January 1, 2013, which increased the maximum corporate income tax rate from 30% to 39%. This rate increase is only applicable to the

EVERTEC, Inc. Notes to Consolidated Financial Statements

fully taxable operations of EVERTEC in Puerto Rico. In addition, Act 40 established a national gross receipts tax based on gross revenues that is included as part of the alternative minimum tax (“AMT”) calculation. On July 1, 2014, the Governor enacted Act 77 introducing a number of substantial amendments, including a deduction for the national gross receipts tax instead of including it as part of the computation of the AMT as previously required by Act 40. On December 22, 2014 the Governor enacted law Act 238 providing a number of technical amendments to Act 77 including the elimination the national gross receipts tax for years 2015 and forward.

As of December 31, 2016, the Company has \$34.0 million of unremitted earnings from foreign subsidiaries. The Company has not recognized a deferred tax liability on undistributed earnings for the Company’s foreign subsidiaries, because these earnings are intended to be indefinitely reinvested. The amount of the unrecognized deferred tax liability depends on judgment required to analyze the withholding tax due, the applicable tax law and factual circumstances in effect at the time of any such distributions, therefore, EVERTEC believes it is not practicable at this time to reliably determine the amount of unrecognized deferred tax liability related to the Company’s undistributed earnings. If circumstances change and it becomes apparent that some or all of the undistributed earnings of a subsidiary will be remitted and income taxes have not been recognized by the parent entity, the parent entity shall accrue as an expense of the current period income taxes attributable to that remittance.

On October 19, 2012, EVERTEC Group was granted an additional tax exemption under the Tax Incentive Act No. 73 of 2008. Under this grant, EVERTEC Group will benefit from a preferential income tax rate on industrial development income, as well as from tax exemptions with respect to its municipal and property tax obligations for certain activities derived from its data processing operations in Puerto Rico. The grant has a term of 15 years effective as of January 1, 2012 with respect to income tax obligations and July 1, 2013 and January 1, 2013 with respect to municipal and property tax obligations, respectively.

The grant establishes a base taxable income amount with respect to EVERTEC Group’s industrial development income, which amount will continue to be subject to the ordinary income tax rate under existing law. Applicable taxable income in excess of the established base taxable income amount will be subject to a preferential rate of 4%. The base taxable income amount will be ratably reduced to zero by the fourth taxable year at which point all of EVERTEC Group’s applicable industrial development income will be taxed at the preferential rate of 4% for the remaining period of the grant.

The grant contains customary commitments, conditions and representations that EVERTEC Group will be required to comply with in order to maintain the grant. The more significant commitments include: (i) maintaining at least 750 employees in EVERTEC Group’s Puerto Rico data processing operations during 2012 and at least 700 employees for the remaining years of the grant, (ii) investing at least \$200.0 million in building, machinery, equipment or computer programs to be used in Puerto Rico during the effective term of the grant (to be made over four year capital investment cycles in \$50.0 million increments); and (iii) 80% of EVERTEC Group employees must be residents of Puerto Rico. Failure to meet the requirements could result, among other things, in reductions in the benefits of the grant or revocation of the grant in its entirety, which could result in EVERTEC, Inc. paying additional taxes or other payments relative to what such parties would be required to pay if the full benefits of the grant are available.

On October 11, 2011, the Puerto Rico Government approved a grant under Tax Incentive Law No. 73 of 2008, retroactively to December 1, 2009. Under this grant, activities derived from consulting and data processing services provided outside Puerto Rico are subject to a preferred rate that declines gradually from 7% to 4% by December 1, 2013. After this date, the rate remains at 4% until its expiration in November 30, 2024.

In addition, EVERTEC Group has a base tax rate of 7% on income derived from certain development and installation service in excess of a determined income for a 10-year period from January 1, 2008.

EVERTEC, Inc. Notes to Consolidated Financial Statements

The following table presents the components of the Company’s deferred tax assets and liabilities:

<i>(Dollar amounts in thousands)</i>	December 31,	
	2016	2015
Deferred tax assets (“DTA”)		
Allowance for doubtful accounts	\$ 265	\$ 420
Unearned Income	2,023	1,315
Investment in equity investee	385	292
Alternative minimum tax	176	400
Share based compensation	697	379
Debt Issuance Costs	127	—
General Reserves	474	87
Derivative liability	172	—
Other temporary assets	704	592
Total gross deferred tax assets	5,023	3,485
Deferred tax liabilities (“DTL”)		
Deferred compensation	\$ 1,458	\$ 1,270
Difference between the assigned values and the tax basis of assets and liabilities recognized in purchase	17,738	21,144
Total gross deferred tax liabilities	19,196	22,414
Deferred tax liability, net	\$(14,173)	\$(18,929)

Pursuant to the provision of the PR Code, net operating losses (“NOL”) can be carried forward for a period of seven, ten or twelve taxable years, depending on the taxable year generated. The Company incurred NOLs during 2010, which will expire in 2022, and in 2013, that will expire in 2023. Act 72 of May 29, 2015, limited the amount of NOLs deduction to 80% for regular tax and 70% for AMT for the taxable year ended December 31, 2016. At December 31, 2016, the Company has \$4.4 million NOL carryforwards for tax purposes available to offset future taxable income. As a result of certain realization requirements of ASC 718, the table of deferred tax assets and liabilities does not include certain windfall tax benefit as of December 31, 2016, and December 31, 2015, that arose directly from tax deductions related to equity compensation greater than compensation recognized for financial reporting. Equity will be increased by \$4.2 million if and when such windfall tax benefit is ultimately realized. The Company uses tax law ordering when determining when windfall tax benefits have been realized.

The Company recognizes the benefit of uncertain tax positions only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement.

The following is a tabular reconciliation of the total amounts of UTBs:

<i>(Dollar amounts in thousands)</i>	Years ended December 31,		
	2016	2015	2014
Balance, beginning of year	\$12,847	\$19,859	\$20,616
Gross increases—tax positions in prior period	—	53	—
Gross decreases—tax positions in prior period	(345)	—	(757)
Lapse of statute of limitations	(283)	(7,065)	—
Balance, end of year	12,219	12,847	19,859

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As of December 31, 2016, 2015 and 2014, approximately \$12.2 million for all years would affect the Company's effective income tax rate, if recognized.

The Company recognizes interest and penalties related to UTB as part of income tax expense. During the years ended December 31, 2016, 2015 and 2014, the Company recognized an income tax expense of \$0.7 million, an income tax benefit of \$2.0 million and an income tax expense of \$1.2 million, respectively, related to interest and penalties. The amount accrued for interest and penalties at December 31, 2016 and 2015 was \$2.0 million, and \$1.3 million, respectively. The Company estimates that it is reasonably possible that the liability for uncertain tax position relating to the net operating loss created by transaction costs will decrease by no more than \$4.5 million in the next twelve months as a result of the expiration of the statute of limitations. The Company believes it has sufficient accruals for contingent tax liabilities.

In connection with tax return examinations, contingencies can arise that generally result from different interpretations of tax laws and regulations as they pertain to the amount, timing or inclusion of revenues and expenses in taxable income, or the ability to utilize tax credits to reduce income taxes payable. While it is probable, based on the potential outcome of the Company's Puerto Rico and foreign tax examinations or the expiration of the statute of limitations for specific jurisdictions, that the liability for UTBs may increase or decrease within the next twelve months, the Company does not expect any such change would have a material effect on our financial condition, results of operations or cash flow.

The Company and its subsidiaries are subject to Puerto Rico income tax as well as income tax of multiple foreign jurisdictions. A significant majority of the income tax is from Puerto Rico with a statute of limitations of four years after filing the income tax returns; therefore, the income tax returns for 2012, 2013, 2014, and 2015 are currently open for examination.

The income tax expense differs from the amount computed by applying the Puerto Rico statutory income tax rate to the income before income taxes as a result of the following:

	<u>Years ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
<i>(Dollar amounts in thousands)</i>			
Computed income tax at statutory rates	\$ 32,525	\$ 31,996	\$ 29,435
Benefit of net tax-exempt interest income	(52)	(284)	—
Differences in tax rates due to multiple jurisdictions	32	37	(942)
Tax (benefit) expense due to a change in estimate	258	(201)	(916)
Adjustment to deferred taxes due to changes in enacted tax rate and tax grant	—	—	(731)
Effect of net disallowed operating losses in foreign entities	—	103	83
Effect of income subject to tax-exemption grant	(24,866)	(23,375)	(19,858)
Unrecognized tax benefit	373	(11,626)	1,830
Other	1	15	—
Income tax expense (benefit)	<u>\$ 8,271</u>	<u>\$ (3,335)</u>	<u>\$ 8,901</u>

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Note 19—Net Income Per Common Share

The reconciliation of the numerator and the denominator of the earnings per common share is as follows:

	Years ended December 31,		
	2016	2015	2014
<i>(Dollar amounts in thousands, except per share data)</i>			
Net income attributable to EVERTEC, Inc.'s common stockholders	\$ 75,036	\$ 85,377	\$ 66,157
Less: non-forfeitable dividends on restricted stock	12	9	—
Net income available to common shareholders	\$ 75,024	\$ 85,368	\$ 66,157
Weighted average common shares outstanding	74,132,863	77,066,459	78,337,152
Weighted average potential dilutive common shares ⁽¹⁾	340,506	114,664	553,987
Weighted average common shares outstanding— assuming dilution	74,473,369	77,181,123	78,891,139
Net income per common share—basic	\$ 1.01	\$ 1.11	\$ 0.84
Net income per common share—diluted	\$ 1.01	\$ 1.11	\$ 0.84

- ⁽¹⁾ Potential common shares consist of common stock issuable under the assumed exercise of stock options, restricted stock and RSUs awards using the treasury stock method.

Refer to Note 14 for a detail of dividends declared and paid during 2016 and 2015.

Note 20—Related Party Transactions

The following table presents the Company's transactions with related parties for each of the periods presented below:

	Years ended December 31,		
	2016	2015	2014
<i>(Dollar amounts in thousands)</i>			
Total revenues ⁽¹⁾⁽²⁾	\$176,473	\$169,433	\$164,336
Cost of revenues	\$ 2,180	\$ 1,701	\$ 1,946
Rent and other fees	\$ 8,110	\$ 7,880	\$ 7,928
Interest earned from and charged by affiliate			
Interest income	\$ 211	\$ 206	\$ 197

- ⁽¹⁾ Total revenues from Popular as a percentage of revenues were 45% for each of the periods presented above.
⁽²⁾ Includes revenues generated from investee accounted for under the equity method of \$2.1 million, \$2.1 million and \$2.5 million for the years ended December 31, 2016, 2015 and 2014, respectively.

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At December 31, 2016 and 2015, the Company had the following balances arising from transactions with related parties:

<i>(Dollar amounts in thousands)</i>	December 31,	
	2016	2015
Cash and restricted cash deposits in affiliated bank	<u>\$15,918</u>	<u>\$23,872</u>
Other due/to from affiliate		
Accounts receivable	<u>\$21,461</u>	<u>\$20,196</u>
Prepaid expenses and other assets	<u>\$ 699</u>	<u>\$ 867</u>
Other long-term assets	<u>\$ 554</u>	<u>\$ —</u>
Accounts payable	<u>\$ 6,300</u>	<u>\$ 2,687</u>
Unearned income	<u>\$14,383</u>	<u>\$11,970</u>
Other long-term liabilities	<u>\$ —</u>	<u>\$ 14</u>

The balance of cash and restricted cash deposits in an affiliated bank was included within the cash and restricted cash line items in the accompanying consolidated balance sheets. Due from affiliates mainly included the amounts outstanding related to processing and information technology services billed to Popular subsidiaries according to the terms of the Master Services Agreement (“MSA”) under which EVERTEC Group has a contract to provide such services for at least 15 years on an exclusive basis for the duration of the agreement on commercial terms consistent with historical pricing practices among the parties. This amount was included in the accounts receivable, net in the consolidated balance sheets.

Note 21—Commitments and Contingencies

The Company leases certain facilities and equipment under operating leases. Most leases contain renewal options for varying periods. Future minimum rental payments on such operating leases at December 31, 2016 are as follows:

<i>(Dollar amounts in thousands)</i>	Unrelated parties	Related party	Minimum future rentals to related parties and unrelated parties
2017	\$402	\$ 6,569	\$ 6,971
2018	124	6,775	6,899
2019	67	6,987	7,054
2020	—	2,144	2,144
2021 and thereafter	—	404	404
	<u>\$593</u>	<u>\$22,879</u>	<u>\$23,472</u>

Certain lease agreements contain provisions for future rent increases. The total amount of rental payments due over the lease term is being charged to rent expense on the straight-line method over the term of the lease. The difference between rent expense recorded and the amount paid is recorded as a deferred rent obligation. There was no deferred rent obligation as of December 31, 2016.

Rent expense of office facilities and real estate for the years ended December 31, 2016, 2015 and 2014 amounted to \$8.2 million, \$8.1 million and \$8.2 million, respectively. Also, rent expense for telecommunications and other equipment for the years ended December 31, 2016, 2015 and 2014 amounted to \$6.2 million, \$5.4 million and \$6.1 million, respectively.

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EVERTEC is a defendant in a number of legal proceedings arising in the ordinary course of business. Based on the opinion of legal counsel, management believes that the final disposition of these matters will not have a material adverse effect on the business, results of operations or financial condition of the Company. The Company has identified certain claims in which a loss may be incurred, but in the aggregate the loss would be minimal. For other claims, where the proceedings are in an initial phase, the Company is unable to estimate the range of possible loss for such legal proceedings. However, the Company at this time believes that any loss related to these latter claims will not be material.

Note 22—Segment Information

The Company operates in three business segments: Merchant Acquiring, Payment Processing and Business Solutions.

The Merchant Acquiring segment consists of revenues from services that allow merchants to accept electronic methods of payment. In the Merchant Acquiring segment, revenues include a discount fee and membership fees charged to merchants, debit network fees and rental fees from POS devices and other equipment, net of credit card interchange and assessment fees charged by credit cards associations (such as VISA or MasterCard) or payment networks. The discount fee is generally a percentage of the transaction value. EVERTEC also charges merchants for other services that are unrelated to the number of transactions or the transaction value.

The Payment Processing segment revenues are comprised of revenues related to providing access to the ATH network and other card networks to financial institutions, including related services such as authorization, processing, management and recording of ATM and POS transactions, and ATM management and monitoring. Payment Processing revenues also include revenues from card processing services (such as credit and debit card processing, authorization and settlement and fraud monitoring and control to debit or credit issuers), payment processing services (such as payment and billing products for merchants, businesses and financial institutions) and EBT (which principally consist of services to the government of Puerto Rico for the delivery of benefits to participants).

For ATH network and processing services, revenues are primarily driven by the number of transactions processed. Revenues are derived primarily from network fees, transaction switching and processing fees, and the leasing POS devices. For card issuer processing, revenues are primarily dependent upon the number of cardholder accounts on file, transactions and authorizations processed, the number of cards embossed and other processing services. For EBT services, revenues are primarily derived from the number of beneficiaries on file.

The Business Solutions segment consists of revenues from a full suite of business process management solutions in various product areas such as core bank processing, network hosting and management, IT professional services, business process outsourcing, item processing, cash processing, and fulfillment. Core bank processing and network services revenues are derived in part from a recurrent fee and from fees based on the number of accounts on file (i.e. savings or checking accounts, loans, etc.) or computer resources utilized. Revenues from other processing services within the Business Solutions segment are generally volume-based and depend on factors such as the number of accounts processed. In addition, EVERTEC is a reseller of hardware and software products and these resale transactions are generally one-time transactions.

The Company's business segments are organized based on the nature of products and services. The CODM reviews their separate financial information to assess performance and to allocate resources.

Management evaluates the operating results of each of its reportable segments based upon revenues and operating income. Segment asset disclosure is not used by the CODM as a measure of segment performance since the segment evaluation is driven by earnings. As such, segment assets are not disclosed in the notes to the accompanying consolidated financial statements.

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The following tables set forth information about the Company's operations by its three business segments for the periods indicated:

<i>(Dollar amounts in thousands)</i>	<u>Merchant Acquiring, net</u>	<u>Payment Processing</u>	<u>Business Solutions</u>	<u>Other</u>	<u>Total</u>
Year ended December 31, 2016					
Revenues	\$91,248	\$144,366	\$186,752	\$(32,859) ⁽¹⁾	\$389,507
Income from operations	31,051	52,071	56,794	(32,771) ⁽²⁾	107,145
Year ended December 31, 2015					
Revenues	85,411	136,566	179,797	(28,246) ⁽¹⁾	373,528
Income from operations	36,466	55,429	50,200	(38,735) ⁽²⁾	103,360
Year ended December 31, 2014					
Revenues	79,136	131,381	177,939	(26,668) ⁽¹⁾	361,788
Income from operations	34,362	58,796	48,299	(44,470) ⁽²⁾	96,987

⁽¹⁾ Represents the elimination of intersegment revenues for services provided by the Payment Processing segment to the Merchant Acquiring segment, and other miscellaneous intersegment revenues.

⁽²⁾ Primarily represents non-operating depreciation and amortization expenses generated as a result of the Merger and certain non-recurring fees and expenses.

The reconciliation of income from operations to consolidated net income is as follows:

<i>(Dollar amounts in thousands)</i>	<u>Years ended December 31,</u>		
	<u>2016</u>	<u>2015</u>	<u>2014</u>
Segment income from operations			
Merchant Acquiring	\$ 31,051	\$ 36,466	\$ 34,362
Payment Processing	52,071	55,429	58,796
Business Solutions	56,794	50,200	48,299
Total segment income from operations	139,916	142,095	141,457
Merger related depreciation and amortization and other unallocated expenses ⁽¹⁾	(32,771)	(38,735)	(44,470)
Income from operations	<u>\$107,145</u>	<u>\$103,360</u>	<u>\$ 96,987</u>
Interest expense, net	(24,240)	(23,771)	(25,444)
Earnings of equity method investment	(52)	147	1,140
Other income (expenses)	544	2,306	2,375
Income tax (expense) benefit	(8,271)	3,335	(8,901)
Net income	<u>\$ 75,126</u>	<u>\$ 85,377</u>	<u>\$ 66,157</u>

⁽¹⁾ Primarily represents non-operating depreciation and amortization expenses generated as a result of the Merger and certain non-recurring fees and expenses.

EVERTEC, Inc. Notes to Consolidated Financial Statements

The geographic segment information below is classified based on the geographic location of the Company's subsidiaries:

<i>(Dollar amounts in thousands)</i>	Years ended December 31,		
	2016	2015	2014
Revenues ⁽¹⁾			
Puerto Rico	\$326,073	\$322,319	\$313,228
Caribbean	16,272	12,154	13,752
Latin America	47,162	39,055	34,808
Total revenues	<u>\$389,507</u>	<u>\$373,528</u>	<u>\$361,788</u>

⁽¹⁾ Revenues are based on subsidiaries' country of domicile.

Major customers

For the years ended December 31, 2016, 2015 and 2014, the Company had one major customer which accounted for approximately \$174.4 million or 45%, \$167.3 million or 45% and \$161.8 million or 45%, respectively, of total revenues. See Note 20.

The Company's next largest customer, the Government of Puerto Rico, consolidating all individual agencies and public corporations, represented 7%, 9% and 10% of the Company's total revenues for the years ended December 31, 2016, 2015 and 2014, respectively.

Note 23—Subsequent Events

On February 17, 2017, the Company's Board of Directors declared a regular quarterly cash dividend of \$0.10 per share on the Company's outstanding shares of common stock. The Board anticipates declaring this dividend in future quarters on a regular basis; however future declarations of dividends are subject to board of directors' approval and may be adjusted as business needs or market conditions change. The cash dividend of \$0.10 per share will be paid on March 20, 2017 to stockholders of record as of the close of business on March 1, 2017.

On the same day, EVERTEC Group entered into a share purchase promise agreement (*Contrato de Promesa de Compraventa de Acciones*) by and among Fondo de Inversión Privado Mater, Inversiones San Bernardo SpA, Inversiones Supernova SpA, Inversiones y Asesorías Bayona Limitada, Inversiones Hagerdorn y Morales Limitada, Christian Hagedorn Hitschfeld and Inversiones Vaimaca Limitada (the "Selling Shareholder") to purchase directly or indirectly 100% of the share capital of EFT Group S.A., a Chilean-based company known commercially as PayGroup at a purchase price of approximately CLP 26,918 million, or approximately US \$42 million at current exchange rates, subject to customary adjustments. PayGroup is a payment processing and software company serving primarily financial institutions throughout Latin America.

The transaction is subject to customary closing conditions, including receipt of US federal bank regulatory approval, and a special provision that allows the selling shareholders to terminate the transaction if US federal bank regulatory approval has not been secured by June 12, 2017, in which case EVERTEC must pay a penalty of approximately US \$2 million. Receipt of US federal bank regulatory approval is dependent on factors outside the control of EVERTEC. There is no assurance that such approval will be obtained by June 12, 2017 or at all.

Schedule I

EVERTEC, Inc. Condensed Financial Statements Parent Company Only

Condensed Balance Sheets

	December 31,	
	2016	2015
<i>(Dollar amounts in thousands)</i>		
Assets		
Current assets:		
Cash	\$ 3,278	\$ 1,673
Accounts receivable, net	—	2,068
Prepaid expenses and other assets	377	109
Prepaid income tax	21	—
Deferred tax asset	—	849
Total current assets	3,676	4,699
Investment in subsidiaries, at equity	126,227	119,605
Total assets	<u>\$129,903</u>	<u>\$124,304</u>
Liabilities and stockholders' equity		
Current liabilities:		
Accrued liabilities	\$ 1,697	\$ 221
Accounts payable	79	47
Income tax payable	—	1,111
Total current liabilities	1,776	1,379
Long-term deferred tax liability, net	11,641	15,484
Other long-term liabilities	11,810	9,227
Total liabilities	<u>25,227</u>	<u>26,090</u>
Stockholders' equity:		
Common stock	726	750
Additional paid-in capital	—	9,718
Accumulated earnings	116,341	95,328
Accumulated other comprehensive loss, net of tax	(12,391)	(7,582)
Total equity	<u>104,676</u>	<u>—</u>
Total liabilities and stockholders' equity	<u>\$129,903</u>	<u>\$124,304</u>

Schedule I

Condensed Statements of Income and Comprehensive Income

	Years ended December 31,		
	2016	2015	2014
<i>(Dollar amounts in thousands)</i>			
Non-operating income (expenses)			
Equity in earnings of subsidiaries	\$75,373	\$81,161	\$74,081
Interest income	244	232	227
Other expenses	(1,351)	(1,686)	(1,994)
Income before income taxes	74,266	79,707	72,314
Income tax (benefit) expense	(770)	(5,670)	6,157
Net income	75,036	85,377	66,157
Other comprehensive (loss) income, net of tax			
Foreign currency translation adjustments	(3,360)	(545)	(6,948)
Loss on cash flow hedge	(1,449)	(515)	—
Total comprehensive income	<u>\$70,227</u>	<u>\$84,317</u>	<u>\$59,209</u>

Condensed Statements of Cash Flows

	Years ended December 31,		
	2016	2015	2014
<i>(Dollar amounts in thousands)</i>			
Cash flows from operating activities	<u>\$ 71,795</u>	<u>\$ 86,237</u>	<u>\$ 57,276</u>
Cash flows from financing activities			
Dividends paid	(29,696)	(30,921)	(31,359)
Repurchase of common stock	(39,946)	(54,949)	(26,197)
Statutory minimum withholding taxes paid on share-based compensation	(548)	(306)	(2,001)
Tax windfall benefits on share-based compensation	—	—	3,669
Issuance of common stock	—	—	543
Settlement of stock options	—	—	(1,604)
Net cash used in financing activities	(70,190)	(86,176)	(56,949)
Net increase in cash	1,605	61	327
Cash at beginning of the period	1,673	1,612	1,285
Cash at end of the period	<u>\$ 3,278</u>	<u>\$ 1,673</u>	<u>\$ 1,612</u>