CIGNA CORP
Form 10-Q
October 29, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended September 30, 2010

OR

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

for the transition period from __________ to __________

Commission file number 1-08323

CIGNA Corporation

(Exact name of registrant as specified in its charter)

Delaware	**06-1059331**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Two Liberty Place, 1601 Chestnut Street
Philadelphia, Pennsylvania 19192
(Address of principal executive offices) (Zip Code)
Registrant s telephone number, including area code **(215) 761-1000**
Registrant s facsimile number, including area code **(215) 761-3596**
Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o Smaller Reporting Company o

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

As of October 15, 2010, 270,920,033 shares of the issuer s common stock were outstanding.

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As used herein, CIGNA or the Company refers to one or more of CIGNA Corporation and its consolidated subsidiaries.

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Part I. ***FINANCIAL INFORMATION***
Item 1. ***FINANCIAL STATEMENTS***
CIGNA Corporation
Consolidated Statements of Income

	Unaudited Three Months Ended September 30,		Unaudited Nine Months Ended September 30,	
(In millions, except per share amounts)	**2010**	2009	**2010**	2009
Revenues				
Premiums and fees	**$ 4,621**	$ 3,985	**$ 13,668**	$ 12,049
Net investment income	**280**	263	**829**	752
Mail order pharmacy revenues	**354**	316	**1,053**	944
Other revenues	**(17)**	(61)	**230**	73
Realized investment gains (losses):				
Other-than-temporary impairments on debt securities, net		(16)	**(1)**	(42)
Other realized investment gains	**28**	30	**45**	2
Total realized investment gains (losses)	**28**	14	**44**	(40)
Total revenues	**5,266**	4,517	**15,824**	13,778
Benefits and Expenses				
Health Care medical claims expense	**2,148**	1,698	**6,435**	5,226
Other benefit expenses	**892**	754	**2,748**	2,551
Mail order pharmacy cost of goods sold	**291**	255	**866**	762
GMIB fair value (gain) loss	**22**	(19)	**182**	(215)
Other operating expenses	**1,449**	1,342	**4,268**	4,064
Total benefits and expenses	**4,802**	4,030	**14,499**	12,388
Income from Continuing Operations before Income Taxes	**464**	487	**1,325**	1,390
Income taxes:				
Current	**101**	68	**256**	138
Deferred	**55**	89	**182**	279
Total taxes	**156**	157	**438**	417
Income from Continuing Operations	**308**	330	**887**	973
Income from Discontinued Operations, Net of Taxes				1
Net Income	**308**	330	**887**	974
Less: Net Income Attributable to Noncontrolling Interest	**1**	1	**3**	2

Shareholders Net Income	**$**	**307**	$	329	**$**	**884**	**$**	972
Basic Earnings Per Share:								
Shareholders income from continuing operations	**$**	**1.13**	$	1.20	**$**	**3.23**	$	3.55
Shareholders income from discontinued operations								
Shareholders net income	**$**	**1.13**	$	1.20	**$**	**3.23**	$	3.55
Diluted Earnings Per Share:								
Shareholders income from continuing operations	**$**	**1.13**	$	1.19	**$**	**3.20**	$	3.54
Shareholders income from discontinued operations								
Shareholders net income	**$**	**1.13**	$	1.19	**$**	**3.20**	$	3.54
Dividends Declared Per Share	**$**		$		**$**	**0.040**	$	0.040
Amounts Attributable to CIGNA:								
Shareholders income from continuing operations	**$**	**307**	$	329	**$**	**884**	**$**	971
Shareholders income from discontinued operations								1
Shareholders Net Income	**$**	**307**	$	329	**$**	**884**	$	972

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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CIGNA Corporation
Consolidated Balance Sheets

(In millions, except per share amounts)	**Unaudited As of September 30, 2010**	As of December 31, 2009
Assets		
Investments:		
Fixed maturities, at fair value (amortized cost, $13,488; $12,580)	**$ 15,354**	$ 13,443
Equity securities, at fair value (cost, $139; $137)	**124**	113
Commercial mortgage loans	**3,486**	3,522
Policy loans	**1,577**	1,549
Real estate	**180**	124
Other long-term investments	**670**	595
Short-term investments	**132**	493
Total investments	**21,523**	19,839
Cash and cash equivalents	**1,404**	924
Accrued investment income	**266**	238
Premiums, accounts and notes receivable, net	**1,438**	1,361
Reinsurance recoverables	**6,406**	6,597
Deferred policy acquisition costs	**1,069**	943
Property and equipment	**894**	862
Deferred income taxes, net	**602**	1,029
Goodwill	**3,119**	2,876
Other assets, including other intangibles	**1,460**	1,056
Separate account assets	**7,798**	7,288
Total assets	**$ 45,979**	$ 43,013
Liabilities		
Contractholder deposit funds	**$ 8,532**	$ 8,484
Future policy benefits	**8,460**	8,136
Unpaid claims and claim expenses	**3,985**	3,968
Health Care medical claims payable	**1,300**	921
Unearned premiums and fees	**415**	427
Total insurance and contractholder liabilities	**22,692**	21,936
Accounts payable, accrued expenses and other liabilities	**6,144**	5,797
Short-term debt	**326**	104
Long-term debt	**2,510**	2,436
Nonrecourse obligations	**23**	23
Separate account liabilities	**7,798**	7,288
Total liabilities	**39,493**	37,584

Contingencies Note 18				
Shareholders Equity				
Common stock (par value per share, $0.25; shares issued, 351)		**88**		88
Additional paid-in capital		**2,530**		2,514
Net unrealized appreciation, fixed maturities	**$ 767**		$ 378	
Net unrealized appreciation, equity securities	**3**		4	
Net unrealized depreciation, derivatives	**(21)**		(30)	
Net translation of foreign currencies	**15**		(12)	
Postretirement benefits liability adjustment	**(1,049)**		(958)	
Accumulated other comprehensive loss		**(285)**		(618)
Retained earnings		**9,421**		8,625
Less treasury stock, at cost		**(5,285)**		(5,192)
Total shareholders equity		**6,469**		5,417
Noncontrolling interest		**17**		12
Total equity		**6,486**		5,429
Total liabilities and equity		**$ 45,979**		$ 43,013
Shareholders Equity Per Share		**$ 23.88**		$ 19.75

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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CIGNA Corporation

Consolidated Statements of Comprehensive Income and Changes in Total Equity
(In millions, except per share amounts)

	Unaudited			
Three Months Ended September 30,	**2010**		2009	
	Compre-hensive Income	**Total Equity**	Compre-hensive Income	Total Equity
Common Stock, July 1 and September 30,		**$ 88**		$ 88
Additional Paid-In Capital, July 1,		**2,526**		2,506
Effects of stock issuance for employee benefit plans		**4**		4
Additional Paid-In Capital, September 30,		**2,530**		2,510
Accumulated Other Comprehensive Loss, July 1,		**(539)**		(837)
Net unrealized appreciation, fixed maturities	**$ 198**	**198**	$ 302	302
Net unrealized depreciation, equity securities			(3)	(3)
Net unrealized appreciation on securities	**198**		299	
Net unrealized depreciation, derivatives	**(11)**	**(11)**	(6)	(6)
Net translation of foreign currencies	**66**	**66**	29	29
Postretirement benefits liability adjustment	**1**	**1**	(1)	(1)
Other comprehensive income	**254**		321	
Accumulated Other Comprehensive Loss, September 30,		**(285)**		(516)
Retained Earnings, July 1,		**9,129**		7,986
Shareholders net income	**307**	**307**	329	329
Effects of stock issuance for employee benefit plans		**(15)**		(12)
Retained Earnings, September 30,		**9,421**		8,303
Treasury Stock, July 1,		**(5,228)**		(5,254)
Repurchase of common stock		**(78)**		
Other, primarily issuance of treasury stock for employee benefit plans		**21**		26
Treasury Stock, September 30,		**(5,285)**		(5,228)
Shareholders Comprehensive Income and Shareholders Equity	**561**	**6,469**	650	5,157

Noncontrolling interest, July 1,				**15**				9
Net income attributable to noncontrolling interest		**1**		**1**		1		1
Accumulated other comprehensive income attributable to noncontrolling interest		**1**		**1**		1		1
Noncontrolling interest, September 30,		**2**		**17**		2		11
Total Comprehensive Income and Total Equity	**$**	**563**	**$**	**6,486**	$	652	$	5,168

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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CIGNA Corporation
Consolidated Statements of Comprehensive Income and Changes in Total Equity

(In millions, except per share amounts)

	Unaudited			
Nine Months Ended September 30,	**2010**		2009	
	Compre-hensive Income	**Total Equity**	Compre-hensive Income	Total Equity
Common Stock, January 1 and September 30,		**$ 88**		$ 88
Additional Paid-In Capital, January 1,		**2,514**		2,502
Effects of stock issuance for employee benefit plans		**16**		8
Additional Paid-In Capital, September 30,		**2,530**		2,510
Accumulated Other Comprehensive Loss, January 1,		**(618)**		(1,074)
Implementation effect of updated guidance on other-than-temporary impairments				(18)
Net unrealized appreciation, fixed maturities	**$ 389**	**389**	$ 567	567
Net unrealized depreciation, equity securities	**(1)**	**(1)**	(3)	(3)
Net unrealized appreciation on securities	**388**		564	
Net unrealized appreciation (depreciation), derivatives	**9**	**9**	(14)	(14)
Net translation of foreign currencies	**27**	**27**	43	43
Postretirement benefits liability adjustment	**(91)**	**(91)**	(17)	(17)
Other comprehensive income	**333**		576	
Accumulated Other Comprehensive Loss, September 30,		**(285)**		(516)
Retained Earnings, January 1,		**8,625**		7,374
Shareholders net income	**884**	**884**	972	972
Effects of stock issuance for employee benefit plans		**(77)**		(50)
Implementation effect of updated guidance on other-than-temporary impairments				18
Common dividends declared (per share: $0.04; $0.04)		**(11)**		(11)
Retained Earnings, September 30,		**9,421**		8,303
Treasury Stock, January 1,		**(5,192)**		(5,298)
Repurchase of common stock		**(201)**		

Other, primarily issuance of treasury stock for employee benefit plans		**108**		70
Treasury Stock, September 30,		**(5,285)**		(5,228)
Shareholders Comprehensive Income and Shareholders Equity	**1,217**	**6,469**	1,548	5,157
Noncontrolling interest, January 1,		**12**		6
Net income attributable to noncontrolling interest	**3**	**3**	2	2
Accumulated other comprehensive income attributable to noncontrolling interest	**2**	**2**	3	3
Noncontrolling interest, September 30,	**5**	**17**	5	11
Total Comprehensive Income and Total Equity	**$ 1,222**	**$ 6,486**	$ 1,553	$ 5,168

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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CIGNA Corporation
Consolidated Statements of Cash Flows

	Unaudited Nine Months Ended September 30,	
(In millions)	**2010**	2009
Cash Flows from Operating Activities		
Net income	**$ 887**	$ 974
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**204**	207
Realized investment (gains) losses	**(44)**	40
Deferred income taxes	**182**	279
Gains on sale of businesses (excluding discontinued operations)	**(20)**	(24)
Income from discontinued operations, net of taxes		(1)
Net changes in assets and liabilities, net of non-operating effects:		
Premiums, accounts and notes receivable	**(55)**	(72)
Reinsurance recoverables	**12**	(1)
Deferred policy acquisition costs	**(118)**	(60)
Other assets	**(191)**	350
Insurance liabilities	**409**	(271)
Accounts payable, accrued expenses and other liabilities	**16**	(1,126)
Current income taxes	**38**	(29)
Other, net	**(37)**	3
Net cash provided by operating activities	**1,283**	269
Cash Flows from Investing Activities		
Proceeds from investments sold:		
Fixed maturities	**685**	655
Equity securities	**3**	21
Commercial mortgage loans	**45**	23
Other (primarily short-term and other long-term investments)	**800**	485
Investment maturities and repayments:		
Fixed maturities	**575**	791
Commercial mortgage loans	**60**	44
Investments purchased:		
Fixed maturities	**(2,047)**	(2,257)
Equity securities	**(5)**	(8)
Commercial mortgage loans	**(160)**	(121)
Other (primarily short-term and other long-term investments)	**(473)**	(489)
Property and equipment purchases	**(209)**	(218)
Acquisitions, net of cash acquired	**(332)**	
Net cash used in investing activities	**(1,058)**	(1,074)
Cash Flows from Financing Activities		
Deposits and interest credited to contractholder deposit funds	**1,019**	1,011

Withdrawals and benefit payments from contractholder deposit funds		**(920)**		(946)
Change in cash overdraft position		**38**		82
Net change in short-term debt				(199)
Issuance of long-term debt		**296**		346
Repayment of long-term debt		**(2)**		(2)
Repurchase of common stock		**(201)**		
Issuance of common stock		**31**		9
Common dividends paid		**(11)**		(11)
Net cash provided by financing activities		**250**		290
Effect of foreign currency rate changes on cash and cash equivalents		**5**		9
Net increase (decrease) in cash and cash equivalents		**480**		(506)
Cash and cash equivalents, January 1,		**924**		1,342
Cash and cash equivalents, September 30,	**$**	**1,404**	$	836
Supplemental Disclosure of Cash Information:				
Income taxes paid, net of refunds	**$**	**215**	$	171
Interest paid	**$**	**116**	$	107

The accompanying Notes to the Consolidated Financial Statements are an integral part of these statements.

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CIGNA CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1 Basis of Presentation

The Consolidated Financial Statements include the accounts of CIGNA Corporation and its significant subsidiaries (referred to collectively as the Company). Intercompany transactions and accounts have been eliminated in consolidation. These Consolidated Financial Statements were prepared in conformity with accounting principles generally accepted in the United States of America (GAAP).

The interim consolidated financial statements are unaudited but include all adjustments (including normal recurring adjustments) necessary, in the opinion of management, for a fair statement of financial position and results of operations for the periods reported. The interim consolidated financial statements and notes should be read in conjunction with the Consolidated Financial Statements and Notes in the Company s Form 10-K for the year ended December 31, 2009.

The preparation of interim consolidated financial statements necessarily relies heavily on estimates. This and certain other factors, such as the seasonal nature of portions of the health care and related benefits business as well as competitive and other market conditions, call for caution in estimating full year results based on interim results of operations.

Certain reclassifications have been made to prior period amounts to conform to the current presentation.

Discontinued operations for the nine months ended September 30, 2009 primarily represented a tax benefit associated with a past divestiture related to the completion of the 2005 and 2006 IRS examinations.

Unless otherwise indicated, amounts in these Notes exclude the effects of discontinued operations.

Note 2 Recent Accounting Pronouncements

Deferred acquisition costs. In October 2010, the Financial Accounting Standards Board (FASB) amended guidance (ASC 944) for the accounting of costs related to the acquisition or renewal of insurance contracts to require costs such as certain sales compensation or telemarketing costs that are related to unsuccessful efforts and any indirect costs to be expensed as incurred. This new guidance must be implemented on January 1, 2012 or may be implemented earlier and any changes in the Company s consolidated financial statements may be recognized prospectively for acquisition costs incurred beginning in 2012 or through retrospective adjustment of comparative prior periods. The Company s deferred acquisition costs arise from sales and renewal activities primarily in its International segment and, to a lesser extent, the Health Care and corporate-owned life insurance businesses. The Company is presently evaluating these new requirements to determine the timing, method and potential effects of their implementation.

Variable interest entities. Effective January 1, 2010, the Company adopted the FASB s amended guidance that requires ongoing qualitative analysis to determine whether a variable interest entity must be consolidated based on the entity s purpose and design, the Company s ability to direct the entity s activities that most significantly impact its economic performance, and the Company s right or obligation to participate in that performance (ASC 810). A variable interest entity is insufficiently capitalized or is not controlled by its equity owners through voting or similar rights. These amendments must be applied to qualifying special-purpose entities and troubled debt restructures formerly excluded from such analysis. On adoption and through September 30, 2010, the Company was not required to consolidate any variable interest entities and there were no effects to its results of operations or financial condition. Although consolidation was not required, disclosures about the Company s involvement with variable interest entities have been provided in Note 11.

Transfers of financial assets. Effective January 1, 2010, the Company adopted the FASB s guidance for accounting for transfers of financial assets (ASC 860) that changes the requirements for recognizing the transfer of financial assets and requires additional disclosures about a transferor s continuing involvement in transferred financial assets. The guidance also eliminates the concept of a qualifying special purpose entity when assessing transfers of financial instruments. On adoption, there were no effects to the Company s results of operations or financial condition.

Fair value measurements. The Company adopted the FASB s updated guidance on fair value measurements (ASU 2010-06) in the first quarter of 2010, which requires separate disclosures of significant transfers between levels in the fair value hierarchy. See Note 8 for additional information.

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Other-than-temporary impairments. On April 1, 2009, the Company adopted the FASB s updated guidance for evaluating whether an impairment is other than temporary for fixed maturities with declines in fair value below amortized cost (ASC 320). A reclassification adjustment from retained earnings to accumulated other comprehensive income was required for previously impaired fixed maturities that had a non-credit loss as of the date of adoption, net of related tax effects.

The cumulative effect of adoption increased the Company s retained earnings in the second quarter of 2009 with an offsetting decrease to accumulated other comprehensive income of $18 million, with no overall change to shareholders equity. See Note 9 for information on the Company s other-than-temporary impairments including additional required disclosures.

Note 3 Acquisitions

The Company may from time to time acquire or dispose of assets, subsidiaries or lines of business. Significant transactions are described below.

Vanbreda International. On August 31, 2010, the Company acquired 100% of the voting stock of Vanbreda International NV (Vanbreda International), based in Antwerp, Belgium for a cash purchase price of approximately $410 million. Vanbreda International specializes in providing worldwide medical insurance and employee benefits to intergovernmental and non-governmental organizations, including international humanitarian operations, as well as corporate clients. Vanbreda International s strong presence in Europe complements the Company s position in providing expatriate benefits primarily to corporate clients in North America, as well as Europe and Asia.

In accordance with GAAP, the total estimated purchase price has been allocated on a provisional basis to the tangible and intangible net assets acquired based on management s estimates of their fair values and may change when appraisals are finalized and as additional information becomes available over the next several months. The condensed balance sheet at the acquisition date was estimated as follows:

(In millions)		
Tangible net assets acquired	$	41
Intangible assets (primarily customer relationships)		220
Goodwill		223
Deferred tax liability		(74)
Net assets acquired	$	410

Goodwill is allocated to the International segment. For foreign tax purposes, the acquisition of Vanbreda International is being treated as a stock purchase. Accordingly, goodwill and other intangible assets will not be amortized for foreign tax purposes but may reduce the taxability of earnings repatriated to the U.S. by Vanbreda International. Since the difference between the Belgium and U.S. corporate tax rates is only 1%, U.S. income taxes on repatriated earnings are expected to be immaterial.

The results of Vanbreda International are included in the Company s Consolidated Financial Statements from the date of acquisition. The pro forma effect on total revenues and net income assuming the acquisition had occurred as of January 1, 2009 was not material to the Company s total revenues and shareholders net income for the three months and nine months ended September 30, 2010 or 2009.

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Note 4 Earnings Per Share (EPS)

Basic and diluted earnings per share were computed as follows:

(Dollars in millions, except per share amounts)		Basic		Effect of Dilution		Diluted
Three Months Ended September 30,						
2010						
Shareholders income from continuing operations	**$**	**307**			**$**	**307**
Shares (in thousands):						
Weighted average		**270,497**				**270,497**
Common stock equivalents				**2,343**		**2,343**
Total shares		**270,497**		**2,343**		**272,840**
EPS	**$**	**1.13**	**$**		**$**	**1.13**
2009						
Shareholders income from continuing operations	$	329			$	329
Shares (in thousands):						
Weighted average		274,398				274,398
Common stock equivalents				1,732		1,732
Total shares		274,398		1,732		276,130
EPS	$	1.20	$	(0.01)	$	1.19

(Dollars in millions, except per share amounts)		Basic		Effect of Dilution		Diluted
Nine Months Ended September 30,						
2010						
Shareholders income from continuing operations	**$**	**884**			**$**	**884**
Shares (in thousands):						
Weighted average		**273,748**				**273,748**
Common stock equivalents				**2,395**		**2,395**
Total shares		**273,748**		**2,395**		**276,143**
EPS	**$**	**3.23**	**$**	**(0.03)**	**$**	**3.20**
2009						
Shareholders income from continuing operations	$	971			$	971
Shares (in thousands):						
Weighted average		273,698				273,698
Common stock equivalents				993		993

Total shares	273,698	993	274,691
EPS	$ 3.55	$ (0.01)	$ 3.54

The following outstanding employee stock options were not included in the computation of diluted earnings per share because their effect would have increased diluted earnings per share (antidilutive) as their exercise price was greater than the average share price of the Company s common stock for the period.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In millions)	**2010**	2009	**2010**	2009
Antidilutive options	**6.7**	8.7	**6.2**	10.0

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The Company held 80,096,166 shares of common stock in Treasury as of September 30, 2010, and 77,475,700 shares as of September 30, 2009.

Note 5 Health Care Medical Claims Payable

Medical claims payable for the Health Care segment reflects estimates of the ultimate cost of claims that have been incurred but not yet reported, those which have been reported but not yet paid (reported claims in process) and other medical expense payable, which primarily comprises accruals for provider incentives and other amounts payable to providers. Incurred but not yet reported comprises the majority of the reserve balance as follows:

(In millions)	**September 30, 2010**	December 31, 2009
Incurred but not yet reported	**$ 1,127**	$ 790
Reported claims in process	**158**	114
Other medical expense payable	**15**	17
Medical claims payable	**$ 1,300**	$ 921

Activity in medical claims payable was as follows:

	For the period ended	
(In millions)	**September 30, 2010**	December 31, 2009
Balance at January 1,	**$ 921**	$ 924
Less: Reinsurance and other amounts recoverable	**206**	211
Balance at January 1, net	**715**	713
Incurred claims related to:		
Current year	**6,527**	6,970
Prior years	**(92)**	(43)
Total incurred	**6,435**	6,927
Paid claims related to:		
Current year	**5,514**	6,278
Prior years	**584**	647
Total paid	**6,098**	6,925
Ending Balance, net	**1,052**	715
Add: Reinsurance and other amounts recoverable	**248**	206
Ending Balance	**$ 1,300**	$ 921

Reinsurance and other amounts recoverable reflect amounts due from reinsurers and policyholders to cover incurred but not reported and pending claims for minimum premium products and certain administrative services only business where the right of offset does not exist. See Note 12 for additional information on reinsurance. For the nine months ended September 30, 2010, actual experience differed from the Company s key assumptions resulting in favorable incurred claims related to prior years medical claims payable of $92 million, or 1.3% of the current year incurred claims as reported for the year ended December 31, 2009. Actual completion factors resulted in a reduction in medical claims payable of $49 million, or 0.7% of the current year incurred claims as reported for the year ended December 31, 2009 for the insured book of business. Actual medical cost trend resulted in a reduction in medical claims payable of $43 million, or 0.6% of the current year incurred claims as reported for the year ended December 31, 2009 for the insured book of business.

For the year ended December 31, 2009, actual experience differed from the Company s key assumptions, resulting in favorable incurred claims related to prior years medical claims payable of $43 million, or 0.6% of the current year incurred claims as reported for the year ended December 31, 2008. Actual completion factors resulted in a reduction of the medical claims payable of $21 million, or 0.3% of the current year incurred claims as reported for the year ended December 31, 2008 for the insured book of business. Actual medical cost trend resulted in a reduction of the medical claims payable of $22 million, or 0.3% of the current year incurred claims as reported for the year ended December 31, 2008 for the insured book of business.

The favorable impacts in 2010 and 2009 relating to completion factors and medical cost trend variances are primarily due to the release of the provision for moderately adverse conditions, which is a component of the assumptions for both completion factors and medical cost trend, established for claims incurred related to prior years. This release was substantially offset by the provision for moderately adverse conditions established for claims incurred related to the current year.

The corresponding impact of prior year development on shareholders net income was not material for the nine months ended September 30, 2010 and 2009. The change in the amount of the incurred claims related to prior years in the medical claims payable liability does not directly correspond to an increase or decrease in the Company s shareholders net income recognized for the following reasons:

First, due to the nature of the Company s retrospectively experience-rated business, only adjustments to medical claims payable on experience-rated accounts in deficit affect shareholders net income. An increase or decrease to medical claims payable on accounts in deficit, in effect, accrues to the Company and directly impacts shareholders net income. An account is in deficit when the accumulated medical costs and administrative charges, including profit charges, exceed the accumulated premium received. Adjustments to medical claims payable on accounts in surplus accrue directly to the policyholder with no impact on the Company s shareholders net income. An account is in surplus when the accumulated premium received exceeds the accumulated medical costs and administrative charges, including profit charges.

Second, the Company consistently recognizes the actuarial best estimate of the ultimate liability within a level of confidence, as required by actuarial standards of practice, which require that the liabilities be adequate under moderately adverse conditions. As the Company establishes the liability for each incurral year, the Company ensures that its assumptions appropriately consider moderately adverse conditions. When a portion of the development related to the prior year incurred claims is offset by an increase determined appropriate to address moderately adverse conditions for the current year incurred claims, the Company does not consider that offset amount as having any impact on shareholders net income.

The determination of liabilities for Health Care medical claims payable required the Company to make critical accounting estimates. See Note 2(N) to the Consolidated Financial Statements in the Company s 2009 Form 10-K.

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Note 6 Cost Reduction

As part of its strategy, the Company has undertaken several initiatives to realign its organization and consolidate support functions in an effort to increase efficiency and responsiveness to customers and to reduce costs.

During 2008 and 2009, the Company conducted a comprehensive review to reduce the operating expenses of its ongoing businesses (cost reduction program). As a result, the Company recognized severance-related and real estate charges in other operating expenses as follows:

- during the fourth quarter of 2009, a charge of $20 million pre-tax ($13 million after-tax), for severance resulting from reductions of approximately 470 positions in its workforce;
- during the third quarter of 2009, a charge of $10 million pre-tax ($7 million after-tax), for severance resulting from reductions of approximately 230 positions in its workforce; and
- during the second quarter of 2009, a charge of $14 million pre-tax ($9 million after-tax), for severance resulting from reductions of approximately 480 positions in its workforce. There have been no charges in 2010.

Substantially all of these charges were recorded in the Health Care segment, and are expected to be paid in cash by the end of 2010.

Cost reduction activity, related to the 2009 charges listed above, for 2010 was as follows:

(In millions)	**Severance**	**Real estate**	**Total**
Balance, January 1, 2010	$ 33	$ 8	$ 41
Less:			
First quarter payments	10	1	11
Second quarter payments	8	5	13
Third quarter payments	7	1	8
Balance, September 30, 2010	$ 8	$ 1	$ 9

Note 7 Guaranteed Minimum Death Benefit Contracts

The Company had future policy benefit reserves for guaranteed minimum death benefit (GMDB) contracts of $1.2 billion as of September 30, 2010 and $1.3 billion as of December 31, 2009. The determination of liabilities for GMDB requires the Company to make critical accounting estimates. The Company estimates its liabilities for GMDB exposures using a complex internal model run using many scenarios and based on assumptions regarding lapse, future partial surrenders, claim mortality (deaths that result in claims), interest rates (mean investment performance and discount rate) and volatility. These assumptions are based on the Company s experience and future expectations over the long-term period, consistent with the long-term nature of this product. The Company regularly evaluates these assumptions and changes its estimates if actual experience or other evidence suggests that assumptions should be revised. If actual experience differs from the assumptions (including lapse, future partial surrenders, claim mortality, interest rates and volatility) used in estimating these liabilities, the result could have a material adverse effect on the Company s consolidated results of operations, and in certain situations, could have a material adverse effect on the Company s financial condition.

In 2000, the Company determined that the GMDB reinsurance business was premium deficient because the recorded future policy benefit reserve was less than the expected present value of future claims and expenses less the expected present value of future premiums and investment income using revised assumptions based on actual and expected experience. The Company tests for premium deficiency by reviewing its reserve each quarter using current market conditions and its long-term assumptions. Under premium deficiency accounting, if the recorded reserve is determined insufficient, an increase to the reserve is reflected as a charge to current period income. Consistent with GAAP, the Company does not recognize gains on premium deficient long duration products.

During the third quarter of 2010, the Company performed its periodic review of assumptions resulting in a charge of $52 million pre-tax ($34 million after-tax) to strengthen GMDB reserves. At December 31, 2009, the Company considered the low level of current short-term interest rates in determining the mean investment performance assumption. As of September 30, 2010, current short-term interest rates had declined from the level anticipated at

December 31, 2009, leading the Company to increase reserves. Interest rate risk is not covered by the GMDB equity hedge program discussed below. The Company also updated the lapse assumption for policies that have already taken or may take a significant partial withdrawal, which had a lesser reserve impact.

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In the first quarter of 2009, the Company reported a charge of $73 million pre-tax ($47 million after-tax) to strengthen GMDB reserves. The reserve strengthening primarily reflected an increase in the provision for future partial surrenders due to market declines, adverse volatility-related impacts due to turbulent equity market conditions, and interest rate impacts.

The following provides updates to the Company s long-term assumptions for GMDB since December 31, 2009:

The annual election rates used to estimate the provision for partial surrenders that essentially lock in the death benefit for a particular policy were updated from 0%-22% at December 31, 2009 to 0%-21% at September 30, 2010. The range of rates reflects the variation in the net amount at risk for each policy and whether surrender charges apply.

The volatility assumption is based on a review of historical monthly returns for each key index (e.g. S&P 500) over a period of at least ten years. Volatility represents the dispersion of historical returns compared to the average historical return (standard deviation) for each index. The volatility assumption for equity fund types has been updated from 16%-30% at December 31, 2009 to 16%-26% at September 30, 2010.

The claim mortality assumption has been updated from 70%-75% of the 1994 Group Annuity Mortality table at December 31, 2009 to 65%-89% at September 30, 2010, with 1% annual improvement beginning January 1, 2000 applying to both periods. The update reflects that for certain contracts, a spousal beneficiary is allowed to elect to continue a contract by becoming its new owner, thereby postponing the death claim rather than receiving the death benefit currently. For certain issuers of these contracts, the claim mortality assumption depends on age, gender, and net amount at risk for the policy. Overall assumed claim mortality rates have increased since December 31, 2009.

The lapse rate assumption has been updated from 0%-21% at December 31, 2009 to 0%-24% at September 30, 2010, depending on contract type, policy duration and the ratio of the net amount at risk to account value. Although the upper end of the range has increased, there is also a higher proportion of policies experiencing lower lapse rates, so overall, assumed lapse rates have declined since December 31, 2009.

The assumed mean investment performance for the underlying equity mutual funds considers the Company s GMDB equity hedge program using futures contracts, and is based on the Company s view of average short-term interest rates over future periods, but considers the current level of short-term interest rates. The current level of short-term rates remains below the level anticipated when the impact of the current level of short-term interest rates was last reviewed at December 31, 2009. As a result, in consideration of the current level of short-term rates, the liability was increased as of September 30, 2010.

Activity in future policy benefit reserves for the GMDB business was as follows:

	For the period ended	
(In millions)	**September 30, 2010**	December 31, 2009
Balance at January 1	**$ 1,285**	$ 1,609
Add: Unpaid Claims	**36**	34
Less: Reinsurance and other amounts recoverable	**53**	83
Balance at January 1, net	**1,268**	1,560
Add: Incurred benefits	**44**	(122)
Less: Paid benefits	**94**	170
Ending balance, net	**1,218**	1,268
Less: Unpaid Claims	**39**	36
Add: Reinsurance and other amounts recoverable	**56**	53
Ending balance	**$ 1,235**	$ 1,285

Benefits paid and incurred are net of ceded amounts. Incurred benefits reflect the favorable or unfavorable impact of a rising or falling equity market on the liability, and include the charge discussed above. As discussed below, losses or gains have been recorded in other revenues as a result of the GMDB equity hedge program to reduce equity market exposures.

The aggregate value of the underlying mutual fund investments was $16.0 billion as of September 30, 2010 and $17.2 billion as of December 31, 2009. The death benefit coverage in force was $6.2 billion as of September 30, 2010 and $7.0 billion as of December 31, 2009. The death benefit coverage in force represents the excess of the guaranteed benefit amount over the value of the underlying mutual fund investments for all contractholders (approximately 540,000 as of September 30, 2010 and 590,000 as of December 31, 2009).

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The Company operates a GMDB equity hedge program to substantially reduce the equity market exposures of this business by selling exchange-traded futures contracts, which are expected to rise in value as the equity market declines, and decline in value as the equity market rises. In addition, the Company uses foreign currency futures contracts to reduce the international equity market and foreign currency risks associated with this business. The notional amount of futures contract positions held by the Company at September 30, 2010 was $1.1 billion. The Company recorded in other revenues pre-tax losses of $119 million for the three months and $72 million for the nine months ended September 30, 2010, and pre-tax losses of $161 million for the three months and $232 million for the nine months ended September 30, 2009.

The Company has also written reinsurance contracts with issuers of variable annuity contracts that provide annuitants with certain guarantees related to minimum income benefits (GMIB). All reinsured GMIB policies also have a GMDB benefit reinsured by the Company. See Note 8 for further information.

Note 8 Fair Value Measurements

The Company carries certain financial instruments at fair value in the financial statements including fixed maturities, equity securities, short-term investments and derivatives. Other financial instruments are measured at fair value under certain conditions, such as when impaired.

Fair value is defined as the price at which an asset could be exchanged in an orderly transaction between market participants at the balance sheet date. A liability s fair value is defined as the amount that would be paid to transfer the liability to a market participant, not the amount that would be paid to settle the liability with the creditor.

Fair values are based on quoted market prices when available. When market prices are not available, fair value is generally estimated using discounted cash flow analyses, incorporating current market inputs for similar financial instruments with comparable terms and credit quality. In instances where there is little or no market activity for the same or similar instruments, the Company estimates fair value using methods, models and assumptions that the Company believes a hypothetical market participant would use to determine a current transaction price. These valuation techniques involve some level of estimation and judgment by the Company which becomes significant with increasingly complex instruments or pricing models.

The Company s financial assets and liabilities carried at fair value have been classified based upon a hierarchy defined by GAAP. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). An asset s or a liability s classification is based on the lowest level of input that is significant to its measurement. For example, a financial asset or liability carried at fair value would be classified in Level 3 if unobservable inputs were significant to the instrument s fair value, even though the measurement may be derived using inputs that are both observable (Levels 1 and 2) and unobservable (Level 3).

The Company performs ongoing analyses of prices used to value the Company s invested assets to determine that they represent appropriate estimates of fair value. This process involves quantitative and qualitative analysis including reviews of pricing methodologies, judgments of valuation inputs, the significance of any unobservable inputs, pricing statistics and trends. The Company also performs sample testing of sales values to confirm the accuracy of prior fair value estimates. These procedures are overseen by the Company s investment professionals.

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Financial Assets and Financial Liabilities Carried at Fair Value

The following tables provide information as of September 30, 2010 and December 31, 2009 about the Company s financial assets and liabilities carried at fair value. Similar disclosures for separate account assets, which are also recorded at fair value on the Company s Consolidated Balance Sheets, are provided separately as gains and losses related to these assets generally accrue directly to policyholders.

September 30, 2010

(In millions)	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total**
Financial assets at fair value:				
Fixed maturities:				
Federal government and agency	**$ 136**	**$ 685**	**$ 4**	**$ 825**
State and local government		**2,604**		**2,604**
Foreign government		**1,143**	**19**	**1,162**
Corporate		**9,580**	**368**	**9,948**
Federal agency mortgage-backed		**17**		**17**
Other mortgage-backed		**85**	**5**	**90**
Other asset-backed		**152**	**556**	**708**
Total fixed maturities (1)	**136**	**14,266**	**952**	**15,354**
Equity securities	**3**	**87**	**34**	**124**
Subtotal	**139**	**14,353**	**986**	**15,478**
Short-term investments		**129**	**3**	**132**
GMIB assets (2)			**673**	**673**
Other derivative assets (3)		**21**		**21**
Total financial assets at fair value, excluding separate accounts	**$ 139**	**$ 14,503**	**$ 1,662**	**$ 16,304**
Financial liabilities at fair value:				
GMIB liabilities	**$**	**$**	**$ 1,246**	**$ 1,246**
Other derivative liabilities (3)		**26**		**26**
Total financial liabilities at fair value	**$**	**$ 26**	**$ 1,246**	**$ 1,272**

(1) Fixed maturities includes $683 million of net appreciation required to adjust future policy benefits

for the run-off settlement annuity business including $129 million of appreciation for securities classified in Level 3.

(2) *The GMIB assets represent retrocessional contracts in place from two external reinsurers which cover 55% of the exposures on these contracts.*

(3) *Other derivative assets includes $17 million of interest rate and foreign currency swaps qualifying as cash flow hedges and $4 million of interest rate swaps not designated as accounting hedges. Other derivative liabilities reflect foreign currency and interest rate swaps qualifying as cash flow hedges. See Note 10 for additional information.*

December 31, 2009

(In millions)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial assets at fair value:				
Fixed maturities:				
Federal government and agency	$ 43	$ 527	$ 1	$ 571
State and local government		2,521		2,521
Foreign government		1,056	14	1,070
Corporate		8,241	344	8,585
Federal agency mortgage-backed		34		34
Other mortgage-backed		114	7	121
Other asset-backed		92	449	541
Total fixed maturities (1)	43	12,585	815	13,443
Equity securities	2	81	30	113
Subtotal	45	12,666	845	13,556
Short-term investments		493		493
GMIB assets (2)			482	482
Other derivative assets (3)		16		16
Total financial assets at fair value, excluding separate accounts	$ 45	$ 13,175	$ 1,327	$ 14,547
Financial liabilities at fair value:				
GMIB liabilities	$	$	$ 903	$ 903
Other derivative liabilities (3)		30		30
Total financial liabilities at fair value	$	$ 30	$ 903	$ 933

(1) Fixed maturities includes $274 million of net appreciation required to adjust future policy benefits for the run-off settlement annuity business including $38 million of

appreciation for securities classified in Level 3.

(2) *The GMIB assets represent retrocessional contracts in place from two external reinsurers which cover 55% of the exposures on these contracts.*

(3) *Other derivative assets include $12 million of interest rate and foreign currency swaps qualifying as cash flow hedges and $4 million of interest rate swaps not designated as accounting hedges. Other derivative liabilities reflect foreign currency and interest rate swaps qualifying as cash flow hedges. See Note 10 for additional information.*

Level 1 Financial Assets

Inputs for instruments classified in Level 1 include unadjusted quoted prices for identical assets in active markets accessible at the measurement date. Active markets provide pricing data for trades occurring at least weekly and include exchanges and dealer markets.

Assets in Level 1 include actively-traded U.S. government bonds and exchange-listed equity securities. Given the narrow definition of Level 1 and the Company s investment asset strategy to maximize investment returns, a relatively small portion of the Company s investment assets are classified in this category.

Level 2 Financial Assets and Financial Liabilities

Inputs for instruments classified in Level 2 include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are market observable or can be corroborated by market data for the term of the instrument. Such other inputs include market interest rates and volatilities, spreads and yield curves. An instrument is classified in Level 2 if the Company determines that unobservable inputs are insignificant.

Fixed maturities and equity securities. Approximately 93% of the Company s investments in fixed maturities and equity securities are classified in Level 2 including most public and private corporate debt and equity securities, federal agency and municipal bonds, non-government mortgage-backed securities and preferred stocks. Because many fixed maturities and preferred stocks do not trade daily, fair values are often derived using recent trades of securities with similar features and characteristics. When recent trades are not available, pricing models are used to determine these prices. These models calculate fair values by discounting future cash flows at estimated market interest rates. Such market rates are derived by calculating the appropriate spreads over comparable U.S. Treasury securities, based on the credit quality, industry and structure of the asset. Typical inputs and assumptions to pricing models include, but are not limited to, a combination of benchmark yields, reported trades, issuer spreads, liquidity, benchmark securities, bids, offers, reference data, and industry and economic events. For mortgage-backed securities, inputs and assumptions may also include characteristics of the issuer, collateral attributes, prepayment speeds and credit rating. Nearly all of these instruments are valued using recent trades or pricing models. Less than 1% of the fair value of investments classified in Level 2 represents foreign bonds that are valued, consistent with local market practice, using a single unadjusted market-observable input derived by averaging multiple broker-dealer quotes.

Short-term investments are carried at fair value, which approximates cost. On a regular basis the Company compares market prices for these securities to recorded amounts to validate that current carrying amounts approximate exit prices. The short-term nature of the investments and corroboration of the reported amounts over the holding period support their classification in Level 2.

Other derivatives classified in Level 2 represent over-the-counter instruments such as interest rate and foreign currency swap contracts. Fair values for these instruments are determined using market observable inputs including forward currency and interest rate curves and widely published market observable indices. Credit risk related to the counterparty and the Company is considered when estimating the fair values of these derivatives. However, the Company is largely protected by collateral arrangements with counterparties, and determined that no adjustment for credit risk was required as of September 30, 2010 or December 31, 2009. The nature and use of these other derivatives are described in Note 10.

Level 3 Financial Assets and Financial Liabilities

Certain inputs for instruments classified in Level 3 are unobservable (supported by little or no market activity) and significant to their resulting fair value measurement. Unobservable inputs reflect the Company s best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

The Company classifies certain newly issued, privately placed, complex or illiquid securities, as well as assets and liabilities relating to GMIB, in Level 3.

Fixed maturities and equity securities. Approximately 6% of fixed maturities and equity securities are priced using significant unobservable inputs and classified in this category, including:

(In millions)		**September 30, 2010**		December 31, 2009
Other asset and mortgage-backed securities	**$**	**561**	$	456
Corporate bonds [(1)]		**320**		288
Subordinated loans and private equity investments		**108**		101
Total	**$**	**989**	$	845

(1) As of September 30, 2010, corporate bonds include

$3 million of short-term investments.

Fair values of mortgage and asset-backed securities and corporate bonds are determined using pricing models that incorporate the specific characteristics of each asset and related assumptions including the investment type and structure, credit quality, industry and maturity date in comparison to current market indices, spreads and liquidity of assets with similar characteristics. For mortgage and asset-backed securities, inputs and assumptions to pricing may also include collateral attributes and prepayment speeds. Recent trades in the subject security or similar securities are assessed when available, and the Company may also review published research, as well as the issuer s financial statements, in its evaluation. Subordinated loans and private equity investments are valued at transaction price in the absence of market data indicating a change in the estimated fair values.

Guaranteed minimum income benefit contracts. Because cash flows of the GMIB liabilities and assets are affected by equity markets and interest rates but are without significant life insurance risk and are settled in lump sum payments, the Company reports these liabilities and assets as derivatives at fair value. The Company estimates the fair value of the assets and liabilities for GMIB contracts using assumptions regarding capital markets (including market returns, interest rates and market volatilities of the underlying equity and bond mutual fund investments), future annuitant behavior (including mortality, lapse, and annuity election rates), and non-performance risk, as well as risk and profit charges. As certain assumptions (primarily related to future annuitant behavior) used to estimate fair values for these contracts are largely unobservable, the Company classifies GMIB assets and liabilities in Level 3. The Company considered the following in determining the view of a hypothetical market participant:

that the most likely transfer of these assets and liabilities would be through a reinsurance transaction with an independent insurer having a market capitalization and credit rating similar to that of the Company; and

that because this block of contracts is in run-off mode, an insurer looking to acquire these contracts would have similar existing contracts with related administrative and risk management capabilities.

These GMIB assets and liabilities are estimated with a complex internal model using many scenarios to determine the present value of net amounts expected to be paid, less the present value of net future premiums expected to be received adjusted for risk and profit charges that the Company estimates a hypothetical market participant would require to assume this business. Net amounts expected to be paid include the excess of the expected value of the income benefits over the values of the annuitants accounts at the time of annuitization. Generally, market return, interest rate and volatility assumptions are based on market observable information. Assumptions related to annuitant behavior reflect the Company s belief that a hypothetical market participant would consider the actual and expected experience of the Company as well as other relevant and available industry resources in setting policyholder behavior assumptions. The significant assumptions used to value the GMIB assets and liabilities as of September 30, 2010 were as follows:

The market return and discount rate assumptions are based on the market-observable LIBOR swap curve.

The projected interest rate used to calculate the reinsured income benefits is indexed to the 7-year Treasury Rate at the time of annuitization (claim interest rate) based on contractual terms. That rate was 1.91% at September 30, 2010 and must be projected for future time periods. These projected rates vary by economic scenario and are determined by an interest rate model using current interest rate curves and the prices of instruments available in the market including various interest rate caps and zero-coupon bonds. For a subset of the business, there is a contractually guaranteed floor of 3% for the claim interest rate.

The market volatility assumptions for annuitants underlying mutual fund investments that are modeled based on the S&P 500, Russell 2000 and NASDAQ Composite are based on the market-implied volatility for these indices for three to seven years grading to historical volatility levels thereafter. For the remaining 55% of underlying mutual fund investments modeled based on other indices (with insufficient market-observable data), volatility is based on the average historical level for each index over the past 10 years. Using this approach, volatility ranges from 17% to 34% for equity funds, 4% to 12% for bond funds, and 1% to 2% for money market funds.

The mortality assumption is 70% of the 1994 Group Annuity Mortality table, with 1% annual improvement beginning January 1, 2000.

The annual lapse rate assumption reflects experience that differs by the company issuing the underlying variable annuity contracts. This range has been updated from 2% to 17% at December 31, 2009 to 1% to 19% as of September 30, 2010, and depends on the time since contract issue and the relative value of the guarantee. Although the upper end of the range has increased, there is also a higher proportion of policies experiencing lower lapse rates, so overall, assumed lapse rates have declined since December 31, 2009.

The annual annuity election rate assumption reflects experience that differs by the company issuing the underlying variable annuity contracts and depends on the annuitant s age, the relative value of the guarantee and whether a contractholder has had a previous opportunity to elect the benefit. Immediately after the expiration of the waiting period, the assumed probability that an individual will annuitize their variable annuity contract is up to 80%. For the second and subsequent annual opportunities to elect the benefit, the assumed probability of election is up to 30%. Actual data is still emerging for the Company as well as the industry and the estimates are based on this limited data.

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The nonperformance risk adjustment is incorporated by adding an additional spread to the discount rate in the calculation of both (1) the GMIB liability to reflect a hypothetical market participant s view of the risk of the Company not fulfilling its GMIB obligations, and (2) the GMIB asset to reflect a hypothetical market participant s view of the reinsurers credit risk, after considering collateral. The estimated market-implied spread is company-specific for each party involved to the extent that company-specific market data is available and is based on industry averages for similarly rated companies when company-specific data is not available. The spread is impacted by the credit default swap spreads of the specific parent companies, adjusted to reflect subsidiaries credit ratings relative to their parent company and any available collateral. The additional spread over LIBOR incorporated into the discount rate ranged from 15 to 115 basis points for the GMIB liability and from 20 to 85 basis points for the GMIB reinsurance asset for that portion of the interest rate curve most relevant to these policies.

The risk and profit charge assumption is based on the Company s estimate of the capital and return on capital that would be required by a hypothetical market participant.

The Company regularly evaluates each of the assumptions used in establishing these assets and liabilities by considering how a hypothetical market participant would set assumptions at each valuation date. Capital markets assumptions are expected to change at each valuation date reflecting currently observable market conditions. Other assumptions may also change based on a hypothetical market participant s view of actual experience as it emerges over time or other factors that impact the net liability. If the emergence of future experience or future assumptions differs from the assumptions used in estimating these assets and liabilities, the resulting impact could be material to the Company s consolidated results of operations, and in certain situations, could be material to the Company s financial condition.

GMIB liabilities are reported in the Company s Consolidated Balance Sheets in Accounts payable, accrued expenses and other liabilities. GMIB assets associated with these contracts represent net receivables in connection with reinsurance that the Company has purchased from two external reinsurers and are reported in the Company s Consolidated Balance Sheets in Other assets, including other intangibles.

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Changes in Level 3 Financial Assets and Financial Liabilities Carried at Fair Value

The following tables summarize the changes in financial assets and financial liabilities classified in Level 3 for the three and nine months ended September 30, 2010 and 2009. These tables exclude separate account assets as changes in fair values of these assets accrue directly to policyholders. Gains and losses reported in these tables may include net changes in fair value that are attributable to both observable and unobservable inputs.

For the Three Months Ended September 30, 2010

(In millions)	Fixed Maturities & Equity Securities (2)	GMIB Assets	GMIB Liabilities	GMIB Net
Balance at July 1, 2010	$ 945	$ 658	$ (1,221)	$ (563)
Gains (losses) included in shareholders net income:				
GMIB fair value gain/(loss)		24	(46)	(22)
Other	5			
Total gains (losses) included in shareholders net income	5	24	(46)	(22)
Gains included in other comprehensive income	9			
Gains required to adjust future policy benefits for settlement annuities (1)	30			
Purchases, issuances, settlements, net	(3)	(9)	21	12
Transfers into/(out of) Level 3:				
Transfers into Level 3	27			
Transfers out of Level 3	(24)			
Total transfers into/(out of) Level 3	3			
Balance at September 30, 2010	$ 989	$ 673	$ (1,246)	$ (573)
Total gains (losses) included in income attributable to instruments held at the reporting date	$ 5	$ 24	$ (46)	$ (22)

(1) Amounts do not accrue to shareholders.

(2) Amounts include $3 million of short-term investments.

For the Three Months Ended September 30, 2009

(In millions)	Fixed Maturities & Equity Securities	GMIB Assets	GMIB Liabilities	GMIB Net
Balance at July 1, 2009	$ 923	$ 685	$ (1,224)	$ (539)
Gains (losses) included in shareholders net income:				
GMIB fair value gain/(loss)		(27)	46	19
Other	(9)			
Total gains (losses) included in shareholders net income	(9)	(27)	46	19
Gains included in other comprehensive income	36			
Gains required to adjust future policy benefits for settlement annuities	56			
Purchases, sales, settlements, net	7	(44)	52	8
Transfers into/(out of) Level 3:				
Transfers into Level 3	40			
Transfers out of Level 3	(53)			
Total transfers into/(out of) Level 3	(13)			
Balance at September 30, 2009	$ 1,000	$ 614	$ (1,126)	$ (512)
Total gains (losses) included in income attributable to instruments held at the reporting date	$ (9)	$ (27)	$ 46	$ 19

(1) Amounts do not accrue to shareholders.

For the Nine Months Ended September 30, 2010

(In millions)	**Fixed Maturities & Equity Securities** [2]	**GMIB Assets**	**GMIB Liabilities**	**GMIB Net**
Balance at January 1, 2010	**$ 845**	**$ 482**	**$ (903)**	**$ (421)**
Gains (losses) included in shareholders net income:				
GMIB fair value gain/(loss)		**211**	**(393)**	**(182)**
Other	**17**			
Total gains (losses) included in shareholders net income	**17**	**211**	**(393)**	**(182)**
Gains included in other comprehensive income	**30**			
Gains required to adjust future policy benefits for settlement annuities [1]	**91**			
Purchases, issuances, settlements, net	**(29)**	**(20)**	**50**	**30**
Transfers into/(out of) Level 3:				
Transfers into Level 3	**99**			
Transfers out of Level 3	**(64)**			
Total transfers into/(out of) Level 3	**35**			
Balance at September 30, 2010	**$ 989**	**$ 673**	**$ (1,246)**	**$ (573)**
Total gains (losses) included in income attributable to instruments held at the reporting date	**$ 14**	**$ 211**	**$ (393)**	**$ (182)**

(1) Amounts do not accrue to shareholders.

(2) Amounts include $3 million of short-term investments.

For the Nine Months Ended September 30, 2009

(In millions)	Fixed Maturities & Equity Securities	GMIB Assets	GMIB Liabilities	GMIB Net
Balance at January 1, 2009	$ 889	$ 953	$ (1,757)	$ (804)

Gains (losses) included in shareholders net income:				
GMIB fair value gain/(loss)		(263)	478	215
Other	(19)			
Total gains (losses) included in shareholders net income	(19)	(263)	478	215
Gains included in other comprehensive income	46			
Losses required to adjust future policy benefits for settlement annuities(1)	(51)			
Purchases, issuances, settlements, net	(3)	(76)	153	77
Transfers into/(out of) Level 3:				
Transfers into Level 3	275			
Transfers out of Level 3	(137)			
Total transfers into/(out of) Level 3	138			
Balance at September 30, 2009	$ 1,000	$ 614	$ (1,126)	$ (512)
Total gains (losses) included in income attributable to instruments held at the reporting date	$ (19)	$ (263)	$ 478	$ 215

(1) Amounts do not accrue to shareholders.

As noted in the tables above, total gains and losses included in net income are reflected in the following captions in the Consolidated Statements of Income:

- Realized investment gains (losses) and net investment income for amounts related to fixed maturities and equity securities; and
- GMIB fair value (gain) loss for amounts related to GMIB assets and liabilities.

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Reclassifications impacting Level 3 financial instruments are reported as transfers into or out of the Level 3 category as of the beginning of the quarter in which the transfer occurs. Therefore gains and losses in income only reflect activity for the period the instrument was classified in Level 3.

Transfers into or out of the Level 3 category occur when unobservable inputs, such as the Company s best estimate of what a market participant would use to determine a current transaction price, become more or less significant to the fair value measurement. For the nine months ended September 30, 2009, transfers into Level 3 from Level 2 primarily reflect an increase in the unobservable inputs used to value certain private corporate bonds, principally related to credit risk of the issuers.

The Company provided reinsurance for other insurance companies that offer a guaranteed minimum income benefit, and then retroceded a portion of the risk to other insurance companies. These arrangements with third-party insurers are the instruments still held at the reporting date for GMIB assets and liabilities in the table above. Because these reinsurance arrangements remain in effect at the reporting date, the Company has reflected the total gain or loss for the period as the total gain or loss included in income attributable to instruments still held at the reporting date. However, the Company reduces the GMIB assets and liabilities resulting from these reinsurance arrangements when annuitants lapse, die, elect their benefit, or reach the age after which the right to elect their benefit expires.

Under FASB s guidance for fair value measurements, the Company s GMIB assets and liabilities are expected to be volatile in future periods because the underlying capital markets assumptions will be based largely on market-observable inputs at the close of each reporting period including interest rates and market-implied volatilities.

GMIB fair value losses of $22 million for the three months ended September 30, 2010, and $182 million for the nine months ended September 30, 2010 were primarily due to declining interest rates, partially offset by increases in underlying account values that occurred during the three and nine months ended September 30, 2010.

GMIB fair value gains of $19 million for the three months ended September 30, 2009 were primarily a result of increases in underlying account values during the period and updates to the risk and profit charge estimates, partially offset by decreases in interest rates and experience varying from assumptions. GMIB fair value gains of $215 million for the nine months ended September 30, 2009, were primarily a result of increases in interest rates, increases in underlying account values and updates to the risk and profit charge estimates, partially offset by increases to the annuitization assumption, experience varying from assumptions and updates to the lapse assumption.

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Separate account assets

Fair values and changes in the fair values of separate account assets generally accrue directly to the policyholders and are excluded from the Company s revenues and expenses. As of September 30, 2010 and December 31, 2009 separate account assets were as follows:

September 30, 2010

Quoted Prices in Active