AETNA INC /PA/
Form 10-Q
April 28, 2011

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2011

or

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

For the transition period from _________ to_________

Commission File Number: 1-16095

Aetna Inc.
(Exact name of registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	23-2229683 (I.R.S. Employer Identification No.)
151 Farmington Avenue, Hartford, CT (Address of principal executive offices)	06156 (Zip Code)
Registrant’s telephone number, including area code	(860) 273-0123

(Former name, former address and former fiscal year, if changed since last report) N/A

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. þ Yes ¨ No

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 Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
þ Yes ¨ No

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 the 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 ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

There were 379.5 million shares of the registrant's voting common stock with a par value of $.01 per share outstanding at March 31, 2011.

Aetna Inc.
Form 10-Q
For the Quarterly Period Ended March 31, 2011

Unless the context otherwise requires, references to the terms “we,” “our” or “us” used throughout this Quarterly Report on Form 10-Q (except the Report of Independent Registered Public Accounting Firm on page 25), refer to Aetna Inc. (a Pennsylvania corporation) (“Aetna”) and its subsidiaries (collectively, the “Company”).

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Part I Financial Information

Item 1. Financial Statements

Consolidated Statements of Income
(Unaudited)

(Millions, except per common share data)	For the Three Months Ended March 31, 2011	2010
Revenue:		
Health care premiums	$ 6,750.6	$ 6,895.1
Other premiums	445.3	474.7
Fees and other revenue (1)	899.6	899.8
Net investment income	252.6	275.2
Net realized capital gains	39.7	76.7
Total revenue	8,387.8	8,621.5
Benefits and expenses:		
Health care costs (2)	5,348.0	5,691.0
Current and future benefits	485.5	527.0
Operating expenses:		
Selling expenses	290.7	321.5
General and administrative expenses	1,272.8	1,195.7
Total operating expenses	1,563.5	1,517.2
Interest expense	66.1	60.9
Amortization of other acquired intangible assets	26.3	24.4
Total benefits and expenses	7,489.4	7,820.5
Income before income taxes	898.4	801.0
Income taxes:		
Current	337.3	216.1
Deferred	(24.9)	22.3
Total income taxes	312.4	238.4
Net income	$ 586.0	$ 562.6
Earnings per common share:		
Basic	$ 1.53	$ 1.30
Diluted	$ 1.50	$ 1.28

(1) Fees and other revenue include administrative services contract member co-payments and plan sponsor reimbursements related to our mail order and specialty pharmacy operations of $15.6 million and $20.4 million (net of pharmaceutical and processing costs of $309.3 million and $353.6 million) for the three months ended March 31, 2011 and 2010, respectively.
(2) Health care costs have been reduced by Insured member co-payments related to our mail order and specialty pharmacy operations of $37.1 million and $31.2 million for the three months ended March 31, 2011 and 2010, respectively.

Refer to accompanying Condensed Notes to Consolidated Financial Statements (Unaudited).

Consolidated Balance Sheets

(Millions)	(Unaudited) At March 31, 2011	At December 31, 2010
Assets:		
Current assets:		
Cash and cash equivalents	$ 1,444.4	$ 1,867.6
Investments	2,083.0	2,169.7
Premiums receivable, net	821.1	661.9
Other receivables, net	841.9	692.6
Accrued investment income	202.6	203.4
Collateral received under securities loan agreements	71.8	210.6
Income taxes receivable	-	210.1
Deferred income taxes	279.0	327.0
Other current assets	682.8	651.3
Total current assets	6,426.6	6,994.2
Long-term investments	17,563.2	17,546.3
Reinsurance recoverables	949.4	960.1
Goodwill	5,541.7	5,146.4
Other acquired intangible assets, net	608.9	495.5
Property and equipment, net	521.2	529.3
Deferred income taxes	91.4	29.9
Other long-term assets	732.4	742.4
Separate Accounts assets	5,366.5	5,295.3
Total assets	$ 37,801.3	$ 37,739.4
Liabilities and shareholders' equity:		
Current liabilities:		
Health care costs payable	$ 2,665.5	$ 2,630.9
Future policy benefits	721.7	728.4
Unpaid claims	593.8	593.3
Unearned premiums	404.3	318.7
Policyholders' funds	1,019.3	918.1
Collateral payable under securities loan agreements	71.9	210.8
Short-term debt	85.0	-
Current portion of long-term debt	450.0	899.9
Income taxes payable	111.6	-
Accrued expenses and other current liabilities	2,384.9	2,436.8
Total current liabilities	8,508.0	8,736.9
Future policy benefits	6,247.8	6,276.4
Unpaid claims	1,513.1	1,514.3
Policyholders' funds	1,302.4	1,316.6
Long-term debt, less current portion	3,483.0	3,482.6
Other long-term liabilities	1,177.3	1,226.5
Separate Accounts liabilities	5,366.5	5,295.3
Total liabilities	27,598.1	27,848.6
Commitments and contingencies (Note 14)		
Shareholders' equity:		

Common stock ($.01 par value; 2.7 billion shares authorized; 379.5 million and 384.4 million shares issued and outstanding in 2011 and 2010, respectively) and additional paid-in capital		709.8		651.5
Retained earnings		10,680.6		10,401.9
Accumulated other comprehensive loss		(1,187.2)		(1,162.6)
Total shareholders' equity		10,203.2		9,890.8
Total liabilities and shareholders' equity	$	37,801.3	$	37,739.4

Refer to accompanying Condensed Notes to Consolidated Financial Statements (Unaudited).

Consolidated Statements of Shareholders' Equity
(Unaudited)

(Millions)	Number of Common Shares Outstanding	Common Stock and Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity	Comprehensive Income
Three Months Ended March 31, 2011						
Balance at December 31, 2010	384.4	$ 651.5	$ 10,401.9	$ (1,162.6)	$ 9,890.8	
Comprehensive income:						
Net income	-	-	586.0	-	586.0	$ 586.0
Other comprehensive loss (Note 8):						
Net unrealized losses on securities	-	-	-	(36.5)	(36.5)	
Net foreign currency and derivative gains	-	-	-	2.3	2.3	
Pension and OPEB plans	-	-	-	9.6	9.6	
Other comprehensive loss	-	-	-	(24.6)	(24.6)	(24.6)
Total comprehensive income						$ 561.4
Common shares issued for benefit plans, including tax benefits	1.8	58.4	-	-	58.4	
Repurchases of common shares	(6.7)	(.1)	(249.9)	-	(250.0)	
Dividend declared	-	-	(57.4)	-	(57.4)	
Balance at March 31, 2011	379.5	$ 709.8	$ 10,680.6	$ (1,187.2)	$ 10,203.2	
Three Months Ended March 31, 2010						
Balance at December 31, 2009	430.8	$ 470.1	$ 10,256.7	$ (1,223.0)	$ 9,503.8	
Comprehensive income:						
Net income	-	-	562.6	-	562.6	$ 562.6
Other comprehensive income (Note 8):						
Net unrealized gains on securities	-	-	-	52.4	52.4	
Net foreign currency and derivative losses	-	-	-	(4.6)	(4.6)	
	-	-	-	32.5	32.5	

Pension and OPEB plans						
Other comprehensive income	-	-	-	80.3	80.3	80.3
Total comprehensive income						$ 642.9
Common shares issued for benefit plans, including tax benefits	1.3	29.2	-	-	29.2	
Repurchases of common shares	(7.2)	(.1)	(251.9)	-	(252.0)	
Balance at March 31, 2010	424.9	$ 499.2	$ 10,567.4	$ (1,142.7)	$ 9,923.9	

Refer to accompanying Condensed Notes to Consolidated Financial Statements (Unaudited).

Consolidated Statements of Cash Flows
(Unaudited)

(Millions)	Three Months Ended March 31, 2011	2010
Cash flows from operating activities:		
Net income	$586.0	$562.6
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized capital gains	(39.7)	(76.7)
Depreciation and amortization	106.6	102.3
Equity in earnings of affiliates, net	(18.9)	(11.4)
Stock-based compensation expense	36.8	27.6
Accretion of net investment discount	(1.5)	(11.6)
Changes in assets and liabilities:		
Accrued investment income	.8	(6.8)
Premiums due and other receivables	(286.2)	(93.3)
Income taxes	297.5	235.6
Other assets and other liabilities	(219.3)	(66.1)
Health care and insurance liabilities	114.2	174.7
Other, net	(4.1)	.4
Net cash provided by operating activities	572.2	837.3
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	2,605.2	2,462.2
Cost of investments	(2,456.2)	(2,686.4)
Additions to property, equipment and software	(62.5)	(74.5)
Cash used for acquisition, net of cash acquired	(493.7)	(.1)
Net cash used for investing activities	(407.2)	(298.8)
Cash flows from financing activities:		
Net repayment of long-term debt	(450.0)	-
Net issuance (repayment) of short-term debt	85.0	(1.3)
Deposits and interest credited for investment contracts	1.2	1.6
Withdrawals of investment contracts	(2.1)	(3.7)
Common shares issued under benefit plans	14.6	3.6
Stock-based compensation tax benefits	8.1	(1.0)
Common shares repurchased	(245.0)	(162.0)
Collateral on interest rate swaps	-	(8.9)
Net cash used for financing activities	(588.2)	(171.7)
Net (decrease) increase in cash and cash equivalents	(423.2)	366.8
Cash and cash equivalents, beginning of period	1,867.6	1,203.6
Cash and cash equivalents, end of period	$1,444.4	$1,570.4
Supplemental cash flow information:		
Interest paid	$49.9	$35.0
Income taxes paid	6.6	3.7

Refer to accompanying Condensed Notes to Consolidated Financial Statements (Unaudited).

Condensed Notes to Consolidated Financial Statements
(Unaudited)

1. Organization

We conduct our operations in three business segments:

- Health Care consists of medical, pharmacy benefits management, dental and vision plans offered on both an Insured basis (where we assume all or a majority of the risk for medical and dental care costs) and an employer-funded basis (where the plan sponsor under an administrative services contract ("ASC") assumes all or a majority of this risk). Medical products include point-of-service ("POS"), preferred provider organization ("PPO"), health maintenance organization ("HMO") and indemnity benefit plans. Medical products also include health savings accounts ("HSAs") and Aetna HealthFund®, consumer-directed health plans that combine traditional POS or PPO and/or dental coverage, subject to a deductible, with an accumulating benefit account (which may be funded by the plan sponsor and/or the member in the case of HSAs). We also offer Medicare and Medicaid products and services and specialty products, such as health information exchange technology services, medical management and data analytics services, behavioral health plans and stop loss insurance, as well as products that provide access to our provider network in select markets.

- Group Insurance primarily includes group life insurance products offered on an Insured basis, including basic and supplemental group term life, group universal life, supplemental or voluntary programs and accidental death and dismemberment coverage. Group Insurance also includes (i) group disability products offered to employers on both an Insured and an ASC basis which consist primarily of short-term and long-term disability insurance, (ii) absence management services offered to employers, which include short-term and long-term disability administration and leave management, and (iii) long-term care products that were offered primarily on an Insured basis, which provide benefits covering the cost of care in private home settings, adult day care, assisted living or nursing facilities. We no longer solicit or accept new long-term care customers.

- Large Case Pensions manages a variety of retirement products (including pension and annuity products) primarily for tax qualified pension plans. These products provide a variety of funding and benefit payment distribution options and other services. Large Case Pensions also includes certain discontinued products (refer to Note 16 beginning on page 23 for additional information).

2. Summary of Significant Accounting Policies

Interim Financial Statements
These interim financial statements necessarily rely on estimates, including assumptions as to annualized tax rates. In the opinion of management, all adjustments necessary for a fair statement of results for the interim periods have been made. All such adjustments are of a normal, recurring nature. The accompanying unaudited consolidated financial statements and related notes should be read in conjunction with the consolidated financial statements and related notes presented in our 2010 Annual Report on Form 10-K (our "2010 Annual Report"). Certain financial information that is normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP"), but that is not required for interim reporting purposes, has been condensed or omitted. We have omitted certain footnote disclosures that would substantially duplicate the disclosures in our 2010 Annual Report, unless the information contained in those disclosures materially changed or is required by GAAP. We have evaluated subsequent events from the balance sheet date through the date the financials were issued and determined there were no other items to disclose.

Principles of Consolidation

These unaudited consolidated financial statements have been prepared in accordance with GAAP and include the accounts of Aetna and the subsidiaries that we control. All significant intercompany balances have been eliminated in consolidation.

Future Application of Accounting Standards

Deferred Acquisition Costs

In October 2010, the Financial Accounting Standards Board ("FASB") released new accounting guidance for costs associated with acquiring or renewing insurance contracts. This guidance clarifies that such costs qualify for capitalization when affiliated with the successful acquisition of new and renewed insurance contracts. The new guidance is effective beginning January 1, 2012. Since our acquisition costs related to our Health Care and Group Insurance products are expensed as incurred, we do not expect the adoption of this accounting guidance to have an impact to our financial position or operating results.

Troubled Debt Restructurings

In April 2011, the FASB released new accounting guidance and additional disclosure requirements relating to a creditor's restructuring of receivables including mortgage loans. The new guidance is effective beginning July 1, 2011. Since we have no material problem, restructured or potential problem mortgage loans, we do not expect the adoption of this accounting guidance to have an impact on our financial position or operating results.

3. Acquisition

In January 2011, we acquired Medicity Inc. ("Medicity"), a health information exchange company, for approximately $500 million using available resources. We recorded goodwill related to this transaction of approximately $395 million, a majority of which will not be tax deductible. All of the goodwill related to this acquisition was assigned to our Health Care segment. Refer to Note 6 on page 7 for additional information.

4. Earnings Per Common Share

Basic earnings per share ("EPS") is computed by dividing net income by the weighted average number of common shares outstanding during the reporting period. Diluted EPS is computed in a similar manner, except that the weighted average number of common shares outstanding is adjusted for the dilutive effects of our outstanding stock awards, but only if the effect is dilutive.

The computations of basic and diluted EPS for the three months ended March 31, 2011 and 2010 are as follows:

(Millions, except per common share data)	2011	2010
Net income	$586.0	$562.6
Weighted average shares used to compute basic EPS	383.5	431.4
Dilutive effect of outstanding stock-based compensation awards (1)	7.7	8.2
Weighted average shares used to compute diluted EPS	391.2	439.6
Basic EPS	$1.53	$1.30
Diluted EPS	$1.50	$1.28

(1) Approximately 12.9 million and 18.9 million stock appreciation rights (with exercise prices ranging from $36.87 to $59.76 and $32.11 to $59.76), and approximately .2 million and 5.8 million stock options (with exercise prices ranging from $36.89 to $42.35 and $33.38 to $42.35) were not included in the calculation of diluted EPS for the three months ended March 31, 2011 and 2010, respectively, as their exercise prices were greater than the average market price of Aetna common shares during such periods.

5. Operating Expenses

For the three months ended March 31, 2011 and 2010, selling expenses (which include broker commissions, the variable component of our internal sales force compensation and premium taxes) and general and administrative expenses were as follows:

(Millions)		2011		2010	
Selling expenses	$	290.7	$	321.5	
General and administrative expenses:					
Salaries and related benefits		763.8		767.8	
Other general and administrative expenses		509.0		427.9	(1)
Total general and administrative expenses		1,272.8		1,195.7	
Total operating expenses	$	1,563.5	$	1,517.2	

(1) Includes litigation-related insurance proceeds of $70.0 million for 2010. Refer to the reconciliation of operating earnings to net income in Note 15 beginning on page 22 for additional information.

6. Goodwill and Other Acquired Intangible Assets

The increase in goodwill for the three months ended March 31, 2011 and 2010 were as follows:

(Millions)	2011	2010
Balance, beginning of the period	$5,146.4	$5,146.2
Goodwill acquired:		
Medicity (1)	395.3	-
Horizon Behavioral Services, LLC	-	(.5)
Balance, end of the period (2)	$5,541.7	$5,145.7

(1) Goodwill related to the acquisition of Medicity is considered preliminary, pending the final allocation of purchase price.
(2) At March 31, 2011 and 2010, approximately $5.4 billion and $5.0 billion of goodwill was assigned to the Health Care segment, respectively, and approximately $104 million of goodwill was assigned to the Group Insurance segment at each date.

Other acquired intangible assets at March 31, 2011 and December 31, 2010 were comprised of the following:

(Millions)	Cost	Accumulated Amortization	Net Balance	Amortization Period (Years)
March 31, 2011				
Other acquired intangible assets:				
Provider networks	$ 703.2	$ 406.3	$ 296.9	12-25 (1)
Customer lists	482.2 (2)	278.4	203.8	4-10 (1)
Technology	92.9 (2)	27.4	65.5	3-10
Other	48.4 (2)	28.0	20.4	2-15
Trademarks	22.3	-	22.3	Indefinite
Total other acquired intangible assets	$ 1,349.0	$ 740.1	$ 608.9	
December 31, 2010				
Other acquired intangible assets:				
Provider networks	$ 703.2	$ 398.9	$ 304.3	12-25 (1)
Customer lists	420.4	262.6	157.8	4-10 (1)
Technology	25.3	25.0	.3	3-5
Other	38.1	27.3	10.8	2-15
Trademarks	22.3	-	22.3	Indefinite
Total other acquired intangible assets	$ 1,209.3	$ 713.8	$ 495.5	

(1) The amortization period for our customer lists and provider networks includes an assumption of renewal or extension of these arrangements. At March 31, 2011 and December 31, 2010, the periods prior to next renewal or extension for our provider networks primarily ranged from 1 to 3 years and the period prior to the next renewal or extension for our customer lists is approximately one year. Any cost related to the renewal or extension of these contracts is expensed as incurred.
(2) As a result of our acquisition of Medicity in 2011, we preliminarily assigned $61.8 million to customer lists, $67.6 million to technology and $10.3 million to other.

We estimate annual pretax amortization for other acquired intangible assets for 2011 and over the next five years to be as follows:

(Millions)	
2011	$ 102.3
2012	90.8
2013	81.6
2014	62.4
2015	48.9
2016	46.8

7. Investments

Total investments at March 31, 2011 and December 31, 2010 were as follows:

	March 31, 2011			December 31, 2010		
(Millions)	Current	Long-term	Total	Current	Long-term	Total
Debt and equity securities available for sale	$2,052.1	$ 14,735.4	$ 16,787.5	$ 2,111.9	$ 14,849.7	$ 16,961.6
Mortgage loans	27.6	1,512.6	1,540.2	55.2	1,454.6	1,509.8
Other investments	3.3	1,315.2	1,318.5	2.6	1,242.0	1,244.6
Total investments	$2,083.0	$ 17,563.2	$ 19,646.2	$ 2,169.7	$ 17,546.3	$ 19,716.0

Debt and Equity Securities

Debt and equity securities available for sale at March 31, 2011 and December 31, 2010 were as follows:

(Millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses		Fair Value
March 31, 2011					
Debt securities:					
U.S. government securities	$1,360.5	$68.7	$(.6)		$1,428.6
States, municipalities and political subdivisions	2,263.9	55.1	(40.4)		2,278.6
U.S. corporate securities	6,516.1	497.4	(23.7)		6,989.8
Foreign securities	2,764.2	207.2	(19.4)		2,952.0
Residential mortgage-backed securities	1,043.6	45.0	(2.1)	(1)	1,086.5
Commercial mortgage-backed securities	1,257.7	97.9	(6.7)	(1)	1,348.9
Other asset-backed securities	459.5	17.3	(5.6)	(1)	471.2
Redeemable preferred securities	193.7	13.7	(9.6)		197.8
Total debt securities	15,859.2	1,002.3	(108.1)		16,753.4
Equity securities	35.4	5.4	(6.7)		34.1
Total debt and equity securities (2)	$15,894.6	$1,007.7	$(114.8)		$16,787.5
December 31, 2010					
Debt securities:					
U.S. government securities	$1,293.5	$80.8	$(.6)		$1,373.7
States, municipalities and political subdivisions	2,288.8	54.4	(46.9)		2,296.3
U.S. corporate securities	6,731.5	553.0	(21.9)		7,262.6
Foreign securities	2,667.4	231.1	(21.2)		2,877.3
Residential mortgage-backed securities	1,089.2	53.6	(2.8)	(1)	1,140.0
Commercial mortgage-backed securities	1,226.4	99.5	(13.7)	(1)	1,312.2
Other asset-backed securities	447.6	21.1	(4.8)	(1)	463.9
Redeemable preferred securities	196.7	12.3	(12.7)		196.3
Total debt securities	15,941.1	1,105.8	(124.6)		16,922.3
Equity securities	35.3	5.6	(1.6)		39.3
Total debt and equity securities (2)	$15,976.4	$1,111.4	$(126.2)		$16,961.6

(1) At March 31, 2011 and December 31, 2010, we held securities for which we had recognized a credit-related impairment in the past. For the three months ended March 31, 2011, we released $10.3 million of non-credit related impairments in the statement of income upon the sale of such securities and in the three months ended March 31, 2010, we recognized $6.0 million, net, of non-credit-related impairments in other comprehensive loss related to these securities (as of March 31, 2011 and December 31, 2010, these securities had a net unrealized capital gain of $10.3 million and $3.9 million, respectively).

(2) Investment risks associated with our experience-rated and discontinued products generally do not impact our operating results (refer to Note 16 beginning on page 23 for additional information on our accounting for discontinued products). At March 31, 2011, debt and equity securities with a fair value of $4.0 billion, gross unrealized capital gains of $305.8 million and gross unrealized capital losses of $41.6 million and, at December 31, 2010, debt and equity securities with a fair value of $4.1 billion, gross unrealized capital gains of $339.5 million and gross unrealized capital losses of $38.1 million were included in total debt and equity securities, but support our experience-rated and discontinued products. Changes in net unrealized capital gains (losses) on these securities are not reflected in accumulated other comprehensive loss.

The fair value of debt securities at March 31, 2011 is shown below by contractual maturity. Actual maturities may differ from contractual maturities because securities may be restructured, called or prepaid.

(Millions)	Fair Value
Due to mature:	
Less than one year	$685.1
One year through five years	3,467.8
After five years through ten years	4,993.4
Greater than ten years	4,700.5
Residential mortgage-backed securities	1,086.5
Commercial mortgage-backed securities	1,348.9
Other asset-backed securities	471.2
Total	$16,753.4

Mortgage-Backed and Other Asset-Backed Securities

All of our residential mortgage-backed securities at March 31, 2011 were agency issued (e.g., Government National Mortgage Association, Federal National Mortgage Association and Federal Home Loan Mortgage Corporation) and carry agency guarantees and explicit or implicit guarantees by the U.S. Government. At March 31, 2011, our residential mortgage-backed securities had an average quality rating of AAA and a weighted average duration of 3.4 years.

Our commercial mortgage-backed securities have underlying loans that are dispersed throughout the U.S. Significant market observable inputs used to value these securities include probability of default and loss severity. At March 31, 2011, these securities had an average quality rating of AA+ and a weighted average duration of 3.9 years.

Our other asset-backed securities have a variety of underlying collateral (e.g., automobile loans, credit card receivables and home equity loans). Significant market observable inputs used to value these securities include the unemployment rate, loss severity and probability of default. At March 31, 2011, these securities had an average quality rating of AA and a weighted average duration of 3.3 years.

Unrealized Capital Losses and Net Realized Capital Gains (Losses)

When a debt or equity security is in an unrealized capital loss position, we monitor the duration and severity of the loss to determine if sufficient market recovery can occur within a reasonable period of time. We recognize an other-than-temporary impairment (“OTTI”) on debt securities when we intend to sell a security that is in an unrealized capital loss position or if we determine a credit-related loss has occurred.

Summarized below are the debt and equity securities we held at March 31, 2011 and December 31, 2010 that were in an unrealized capital loss position, aggregated by the length of time the investments have been in that position:

	Less than 12 months		Greater than 12 months		Total (1)	
(Millions)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2011						
Debt securities:						
U.S. government securities	$ 89.5	$ .2	$ 17.6	$ .4	$ 107.1	$ .6
States, municipalities and political subdivisions	816.3	30.5	78.3	9.9	894.6	40.4
U.S. corporate securities	839.6	20.8	119.1	2.9	958.7	23.7
Foreign securities	512.4	13.5	35.5	5.9	547.9	19.4
Residential mortgage-backed securities	188.3	2.0	3.3	.1	191.6	2.1
Commercial mortgage-backed securities	151.6	1.7	48.5	5.0	200.1	6.7
Other asset-backed securities	116.5	2.6	4.7	3.0	121.2	5.6
Redeemable preferred securities	-	-	87.8	9.6	87.8	9.6
Total debt securities	2,714.2	71.3	394.8	36.8	3,109.0	108.1
Equity securities	18.3	5.1	9.5	1.6	27.8	6.7
Total debt and equity securities (1)	$ 2,732.5	$ 76.4	$ 404.3	$ 38.4	$ 3,136.8	$ 114.8
December 31, 2010						
Debt securities:						
U.S. government securities	$ 8.4	$ .2	$ 19.8	$ .4	$ 28.2	$ .6
States, municipalities and political subdivisions	964.9	37.6	82.7	9.3	1,047.6	46.9
U.S. corporate securities	665.8	17.0	210.2	4.9	876.0	21.9
Foreign securities	375.9	14.6	34.6	6.6	410.5	21.2
Residential mortgage-backed securites	103.7	2.6	6.6	.2	110.3	2.8
Commercial mortgage-backed securities	103.7	2.4	78.5	11.3	182.2	13.7
Other asset-backed securities	85.9	2.0	4.9	2.8	90.8	4.8
Redeemable preferred securities	4.5	-	94.3	12.7	98.8	12.7

Total debt securities	2,312.8	76.4	531.6	48.2	2,844.4	124.6
Equity securities	.5	-	9.5	1.6	10.0	1.6
Total debt and equity securities (1)	$ 2,313.3	$ 76.4	$ 541.1	$ 49.8	$ 2,854.4	$ 126.2

(1) At March 31, 2011 and December 31, 2010, debt and equity securities in an unrealized capital loss position of $41.6 million and $38.1 million, respectively, and with related fair value of $765.2 million and $650.5 million, respectively, related to experience-rated and discontinued products.

We reviewed the securities in the tables above and concluded that these are performing assets generating investment income to support the needs of our business. In performing this review, we considered factors such as the quality of the investment security based on research performed by external rating agencies and our internal credit analysts and the prospects of realizing the carrying value of the security based on the investment's current prospects for recovery. At March 31, 2011, we did not have the intention to sell the securities that were in an unrealized capital loss position.

The maturity dates for debt securities in an unrealized capital loss position at March 31, 2011 were as follows:

	Supporting discontinued and experience-rated products		Supporting remaining products		Total	
(Millions)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Due to mature:						
Less than one year	$1.9	$-	$57.3	$1.3	$59.2	$1.3
One year through five years	11.7	.1	342.9	3.2	354.6	3.3
After five years through ten years	190.5	5.3	547.5	11.3	738.0	16.6
Greater than ten years	454.0	27.5	990.3	45.0	1,444.3	72.5
Residential mortgage-backed securities	9.6	.5	182.0	1.6	191.6	2.1
Commercial mortgage-backed securities	42.8	.8	157.3	5.9	200.1	6.7
Other asset-backed securities	27.3	.7	93.9	4.9	121.2	5.6
Total	$737.8	$34.9	$2,371.2	$73.2	$3,109.0	$108.1

Net realized capital gains for the three months ended March 31, 2011 and 2010, excluding amounts related to experience-rated contract holders and discontinued products, were as follows:

(Millions)	2011	2010
OTTI losses on securities	$(2.8)	$(20.2)
Portion of OTTI losses recognized in other comprehensive income	-	6.4
Net OTTI losses on securities recognized in earnings	(2.8)	(13.8)
Net realized capital gains, excluding OTTI losses on securities	42.5	90.5
Net realized capital gains	$39.7	$76.7

The net realized capital gains for the three months ended March 31, 2011 and 2010 were primarily attributable to the sale of debt securities.

Excluding amounts related to experience-rated and discontinued products, proceeds from the sale of debt securities and the related gross realized capital gains and losses for the three months ended March 31, 2011 and 2010 were as follows:

(Millions)	2011	2010
Proceeds on sales	$ 1,514.4	$ 1,590.9
Gross realized capital gains	53.8	108.7
Gross realized capital losses	18.8	8.2

Mortgage loans

Our mortgage loans are collateralized by commercial real estate. During the three months ended March 31, 2011 and 2010 we had the following activity in our mortgage loan portfolio:

(Millions)	2011	2010

New mortgage loans	$ 75.7	$ -
Mortgage loans fully repaid	34.5	14.3
Mortgage loans foreclosed	-	11.5

At March 31, 2011 and December 31, 2010, we had no material problem, restructured or potential problem loans included in mortgage loans. We also had no material reserves on our mortgage loans at March 31, 2011 or December 31, 2010.

We assess our mortgage loans on a regular basis for credit impairments, and annually we assign a credit quality indicator to each loan. Our credit quality indicator is internally developed and categorizes our portfolio on a scale from 1 to 7. Category 1 represents loans of superior quality, and Categories 6 and 7 represent loans where collections are doubtful. Most of our mortgage loans fall into the Level 2 to 4 ratings. These ratings represent loans where credit risk is minimal to acceptable; however, these loans may display some susceptibility to economic changes. Category 5 represents loans where credit risk is not substantial but these loans warrant management's close attention. These indicators are based upon several factors, including current loan to value ratios, property condition, market trends, borrower quality and deal structure. Based upon our most recent assessment at March 31, 2011 and December 31, 2010, our mortgage loans were given the following ratings:

(In millions, except credit ratings indicator)	March 31, 2011	December 31, 2010
1	$ 100.5	$ 99.4
2 to 4	1,325.0	1,301.5
5	92.0	86.1
6 and 7	22.7	22.8
Total	$ 1,540.2	$ 1,509.8

Variable Interest Entities

In determining whether to consolidate a variable interest entity ("VIE"), we consider several factors including whether we have the power to direct activities, the obligation to absorb losses and the right to receive benefits that could potentially be significant to the VIE. We have relationships with certain real estate and hedge fund partnerships that are considered VIEs, but are not consolidated. We record the amount of our investment in these partnerships as long-term investments on our balance sheets and recognize our share of partnership income or losses in earnings. Our maximum exposure to loss as a result of our investment in these partnerships is our investment balance at March 31, 2011 and December 31, 2010 of approximately $159 million and $153 million, respectively, and the risk of recapture of tax credits related to the real estate partnerships previously recognized, which we do not consider significant. We do not have a future obligation to fund losses or debts on behalf of these investments; however, we may voluntarily contribute funds. The real estate partnerships construct, own and manage low-income housing developments and had total assets of approximately $5.1 billion at both March 31, 2011 and December 31, 2010. The hedge fund partnerships had total assets of approximately $6.5 billion and $6.1 billion at March 31, 2011 and December 31, 2010, respectively.

Non-controlling Interests

Certain of our investment holdings are partially-owned by third parties. At March 31, 2011 and December 31, 2010, $78 million and $74 million, respectively, of our investment holdings were owned by third parties. The non-controlling entities' share of these investments was included in accrued expenses and other current liabilities. Net income attributable to these interests was $2 million and $1 million for the three months ended March 31, 2011 and 2010, respectively. These non-controlling interests did not have a material impact on our financial position or operating results.

Net Investment Income

Sources of net investment income for the three months ended March 31, 2011 and 2010 were as follows:

(Millions)	2011	2010
Debt securities	$211.3	$236.4
Mortgage loans	24.7	26.7
Other investments	24.1	18.6
Gross investment income	260.1	281.7
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