HANOVER INSURANCE GROUP, INC.
Form 10-Q
November 04, 2010
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2010

¨ **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 1-13754

THE HANOVER INSURANCE GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**04-3263626**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

440 Lincoln Street, Worcester, Massachusetts 01653

(Address of principal executive offices) (Zip Code)

(508) 855-1000

(Registrant s telephone number, including area code)

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. Yesx 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 Regulation 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). Yes x 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	x	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 ¨ No x

The number of shares outstanding of the registrant s common stock was 45,109,681 as of November 1, 2010.

TABLE OF CONTENTS

Table of Contents

PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

THE HANOVER INSURANCE GROUP, INC.

CONSOLIDATED STATEMENTS OF INCOME

	(Unaudited) Quarter Ended September 30,		(Unaudited) Nine months Ended September 30,	
(In millions except per share data)	**2010**	**2009**	**2010**	**2009**
REVENUES				
Premiums	**$ 728.0**	$ 637.4	**$ 2,092.3**	$ 1,899.4
Net investment income	**61.3**	62.1	**184.2**	188.3
Net realized investment gains (losses):				
Net realized gains from sales and other	**7.1**	6.1	**24.3**	19.6
Total other-than-temporary impairment losses on securities	**(0.2)**	(4.5)	**(3.5)**	(39.1)
Portion of loss transferred (from) to other comprehensive income	**(1.2)**	(1.6)	**(4.0)**	9.8
Net other than temporary impairment losses on securities recognized in earnings	**(1.4)**	(6.1)	**(7.5)**	(29.3)
Total net realized investment gains (losses)	**5.7**	-	**16.8**	(9.7)
Fees and other income	**9.0**	9.0	**25.6**	25.8
Total revenues	**804.0**	708.5	**2,318.9**	2,103.8
LOSSES AND EXPENSES				
Losses and loss adjustment expenses	**454.6**	403.0	**1,384.6**	1,225.1
Policy acquisition expenses	**173.4**	146.8	**490.8**	434.7
Gain from retirement of debt	**-**	(0.2)	**-**	(34.5)
Other operating expenses	**102.9**	91.4	**308.0**	281.1
Total losses and expenses	**730.9**	641.0	**2,183.4**	1,906.4
Income before federal income taxes	**73.1**	67.5	**135.5**	197.4
Federal income tax expense (benefit):				
Current	**21.2**	17.8	**(8.5)**	42.8
Deferred	**0.5**	1.1	**48.2**	22.7
Total federal income tax expense	**21.7**	18.9	**39.7**	65.5
Income from continuing operations	**51.4**	48.6	**95.8**	131.9
Discontinued operations (See Note 3):				
Gain from discontinued FAFLIC business (net of tax benefit of $0.3 and $0.3 for the quarters ended September 30, 2010 and 2009 and $0.3 and $0.3 for the nine months ended September 30, 2010 and 2009)	**0.5**	0.4	**0.4**	6.3

Gain (loss) from operations of discontinued accident and health insurance business (net of income tax benefit (expense) of $0.1 and ($0.4) or the quarters ended September 30, 2010 and 2009 and $0.3 and ($0.5) for the nine months ended September 30, 2010 and 2009)		**0.2**		0.7		**(0.9)**		(2.4)
Gain on disposal of variable life and annuity business		**0.1**		-		**1.0**		4.1
Other discontinued operations		**0.1**		-		**0.1**		-
Net income	**$**	**52.3**	$	49.7	**$**	**96.4**	$	139.9

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

3

Table of Contents

THE HANOVER INSURANCE GROUP, INC.

CONSOLIDATED STATEMENTS OF INCOME (*CONTINUED*)

	(Unaudited) Quarter Ended September 30,		(Unaudited) Nine months Ended September 30,	
	2010	**2009**	**2010**	**2009**
PER SHARE DATA				
Basic				
Income from continuing operations	**$ 1.14**	$ 0.96	**$ 2.09**	$ 2.59
Discontinued operations:				
Gain from discontinued FAFLIC business (net of income tax benefit of $0.01 and $0.01 for the quarters ended September 30, 2010 and 2009 and $0.01 and $0.01 for the nine months ended September 30, 2010 and 2009)	**0.01**	0.01	**0.01**	0.12
Gain (loss) from operations of discontinued accident and health insurance business (net of income tax benefit (expense) of $0.01 and ($0.01) for the quarters ended September 30, 2010 and 2009 and $0.01 and ($0.01) for the nine months ended September 30, 2010 and 2009)	**0.01**	0.01	**(0.02)**	(0.04)
Gain on disposal of variable life insurance and annuity business	**-**	-	**0.03**	0.08
Net income per share	**$ 1.16**	$ 0.98	**$ 2.11**	$ 2.75
Weighted average shares outstanding	**44.9**	50.7	**45.7**	51.0
Diluted				
Income from continuing operations	**$ 1.12**	$ 0.95	**$ 2.06**	$ 2.57
Discontinued operations:				
Gain from discontinued FAFLIC business (net of income tax benefit of $0.01 and $0.01 for the quarters ended September 30, 2010 and 2009 and $0.01 and $0.01 for the nine months ended September 30, 2010 and 2009)	**0.02**	0.01	**0.01**	0.12
Gain (loss) from operations of discontinued accident and health insurance business (net of income tax benefit (expense) of $0.01 and ($0.01) for the quarters ended September 30, 2010 and 2009 and $0.01 and ($0.01) for the nine months ended September 30, 2010 and 2009)	**0.01**	0.01	**(0.02)**	(0.05)
Gain on disposal of variable life insurance and annuity business	**-**	-	**0.03**	0.08
Net income per share	**$ 1.15**	$ 0.97	**$ 2.08**	$ 2.72
Weighted average shares outstanding	**45.7**	51.2	**46.4**	51.4

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC .

CONSOLIDATED BALANCE SHEETS

(In millions, except per share data)		**(Unaudited) September 30, 2010**		**December 31, 2009**
ASSETS				
Investments:				
Fixed maturities, at fair value (amortized cost of $4,588.8 and $4,520.3)	**$**	**4,904.6**	$	4,615.6
Equity securities, at fair value (cost of $112.3 and $57.3)		**125.7**		69.2
Mortgage loans and other long-term investments		**41.2**		32.3
Total investments		**5,071.5**		4,717.1
Cash and cash equivalents		**271.6**		316.5
Accrued investment income		**53.5**		52.3
Premiums, accounts and notes receivable, net		**807.8**		590.8
Reinsurance receivable on paid and unpaid losses and ceded unearned premiums		**1,230.3**		1,197.9
Deferred policy acquisition costs		**346.0**		286.3
Deferred federal income taxes		**116.2**		228.6
Goodwill		**179.4**		171.4
Other assets		**386.3**		351.2
Assets of discontinued operations		**134.1**		130.6
Total assets	**$**	**8,596.7**	$	8,042.7
LIABILITIES				
Policy liabilities and accruals:				
Losses and loss adjustment expenses	**$**	**3,232.1**	$	3,153.9
Unearned premiums		**1,553.6**		1,300.5
Total policy liabilities and accruals		**4,785.7**		4,454.4
Expenses and taxes payable		**523.7**		603.2
Reinsurance premiums payable		**33.2**		58.5
Long-term debt		**640.0**		433.9
Liabilities of discontinued operations		**135.3**		134.1
Total liabilities		**6,117.9**		5,684.1
Commitments and contingencies (Note 14)				
SHAREHOLDERS EQUITY				
Preferred stock, $0.01 par value, 20.0 million shares authorized, none issued		**-**		-
Common stock, $0.01 par value, 300.0 million shares authorized, 60.5 million shares issued		**0.6**		0.6
Additional paid-in capital		**1,798.6**		1,808.5

Accumulated other comprehensive income		**203.2**		28.8
Retained earnings		**1,201.3**		1,141.1
Treasury stock at cost (15.6 and 13.0 million shares)		**(724.9)**		(620.4)
Total shareholders equity		**2,478.8**		2,358.6
Total liabilities and shareholders equity	**$**	**8,596.7**	$	8,042.7

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

	(Unaudited) Nine months Ended September 30,	
(In millions)	**2010**	**2009**
PREFERRED STOCK		
Balance at beginning and end of period	**$ -**	$ -
COMMON STOCK		
Balance at beginning and end of period	**0.6**	0.6
ADDITIONAL PAID-IN CAPITAL		
Balance at beginning of period	**1,808.5**	1,803.8
Employee and director stock-based awards and other	**(9.9)**	4.0
Balance at end of period	**1,798.6**	1,807.8
ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)		
NET UNREALIZED APPRECIATION (DEPRECIATION) ON INVESTMENTS:		
Balance at beginning of period	**107.7**	(276.1)
Cumulative effect of change in accounting principle	**-**	(33.3)
Balance at beginning of period, as adjusted	**107.7**	(309.4)
Net appreciation during the period:		
Net appreciation on available-for-sale securities	**227.1**	428.8
(Provision) benefit for deferred federal income taxes	**(57.4)**	(30.2)
	169.7	398.6
Balance at end of period	**277.4**	89.2
DEFINED BENEFIT PENSION AND POSTRETIREMENT PLANS:		
Balance at beginning of period	**(78.9)**	(108.7)
Amounts arising in the period	**-**	(1.6)
Amortization during the period:		
Amount recognized as net periodic benefit cost	**7.3**	14.9
Provision for deferred federal income taxes	**(2.6)**	(4.6)
	4.7	8.7
Balance at end of period	**(74.2)**	(100.0)
Total accumulated other comprehensive income (loss)	**203.2**	(10.8)

RETAINED EARNINGS				
Balance at beginning of period		**1,141.1**		949.8
Cumulative effect of change in accounting principle		**-**		33.3
Balance at beginning of period, as adjusted		**1,141.1**		983.1
Net income		**96.4**		139.9
Dividends to shareholders		**(35.9)**		-
Treasury stock issued for less than cost		**(7.9)**		(4.1)
Recognition of share-based compensation		**7.6**		2.5
Balance at end of period		**1,201.3**		1,121.4
TREASURY STOCK				
Balance at beginning of period		**(620.4)**		(482.2)
Shares purchased at cost		**(126.0)**		(36.2)
Net shares reissued at cost under employee stock-based compensation plans		**21.5**		6.5
Balance at end of period		**(724.9)**		(511.9)
Total shareholders equity	**$**	**2,478.8**	$	2,407.1

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In millions)	(Unaudited) Quarter Ended September 30, 2010	(Unaudited) Quarter Ended September 30, 2009	(Unaudited) Nine months Ended September 30, 2010	(Unaudited) Nine months Ended September 30, 2009
Net income	**$ 52.3**	49.7	**$ 96.4**	$ 139.9
Other comprehensive income:				
Available-for-sale securities:				
Net appreciation during the period	**101.4**	189.4	**227.1**	428.8
Provision for deferred federal income taxes	**(25.9)**	(30.4)	**(57.4)**	(30.2)
Total available-for-sale securities	**75.5**	159.0	**169.7**	398.6
Pension and postretirement benefits:				
Amounts arising in the period	**-**	-	**-**	(1.6)
Amortization recognized as net periodic benefit costs:				
Net actuarial loss	**4.3**	6.8	**12.9**	20.4
Prior service cost	**(1.5)**	(1.5)	**(4.4)**	(4.3)
Transition asset	**(0.4)**	(0.4)	**(1.2)**	(1.2)
Total amortization recognized as net periodic benefit costs	**2.4**	4.9	**7.3**	14.9
Provision for deferred federal income taxes	**(0.9)**	(1.7)	**(2.6)**	(4.6)
Total pension and postretirement benefits	**1.5**	3.2	**4.7**	8.7
Other comprehensive income	**77.0**	162.2	**174.4**	407.3
Comprehensive income	**$ 129.3**	$ 211.9	**$ 270.8**	$ 547.2

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Unaudited)	
	Nine months Ended September 30,	
(In millions)	**2010**	**2009**
Cash flows from operating activities		
Net income	**$ 96.4**	$ 139.9
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Gain on disposal of variable life insurance and annuity business	**(1.0)**	(4.1)
Gain from sale of FAFLIC	**(0.4)**	(6.3)
Gain from retirement of debt	**-**	(34.5)
Net realized investment (gains) losses	**(16.4)**	13.0
Net amortization and depreciation	**12.0**	9.0
Stock-based compensation expense	**8.6**	8.9
Amortization of deferred benefit plan costs	**7.4**	14.9
Deferred federal income taxes	**48.1**	22.7
Change in deferred acquisition costs	**(58.5)**	(20.4)
Change in premiums and notes receivable, net of reinsurance premiums payable	**(241.9)**	(35.1)
Change in accrued investment income	**(0.9)**	(1.2)
Change in policy liabilities and accruals, net	**276.2**	(36.5)
Change in reinsurance receivable	**(14.7)**	27.2
Change in expenses and taxes payable	**(104.6)**	(80.8)
Other, net	**(25.3)**	10.2
Net cash (used in) provided by operating activities	**(15.0)**	26.9
Cash flows from investing activities		
Proceeds from disposals and maturities of available-for-sale fixed maturities	**998.6**	1,749.2
Proceeds from disposals of equity securities and other investments	**36.1**	1.4
Proceeds from mortgages sold, matured or collected	**8.8**	10.7
Proceeds from the sale of FAFLIC	**-**	105.8
Cash transferred with sale of FAFLIC	**-**	(108.1)
Purchase of available-for-sale fixed maturities	**(981.7)**	(2,078.4)
Purchase of other investments	**(95.3)**	(31.0)
Net cash used for business acquisitions	**(13.3)**	-
Capital expenditures	**(6.6)**	(6.6)
Other investing items	**-**	1.5
Net cash used in investing activities	**(53.4)**	(355.5)
Cash flows from financing activities		
Exercise of options	**9.3**	1.6
Proceeds from long term debt	**205.6**	125.0
Change in collateral related to securities lending program	**(23.4)**	75.8
Dividends paid to shareholders	**(35.9)**	-
Repurchase of long-term debt	**(0.4)**	(125.9)
Repurchases of common stock	**(130.6)**	(36.1)

Other financing activities	**0.1**	0.1
Net cash provided by financing activities	**24.7**	40.5
Net change in cash and cash equivalents	**(43.7)**	(288.1)
Net change in cash related to discontinued operations	**(1.2)**	123.6
Cash and cash equivalents, beginning of period	**316.5**	397.7
Cash and cash equivalents, end of period	**$ 271.6**	$ 233.2

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

THE HANOVER INSURANCE GROUP, INC.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Principles of Consolidation

The accompanying unaudited consolidated financial statements of The Hanover Insurance Group, Inc. (THG or the Company) have been prepared in accordance with generally accepted accounting principles for interim financial information and with the requirements of Form 10-Q.

The interim consolidated financial statements of THG include the accounts of The Hanover Insurance Company (Hanover Insurance), and Citizens Insurance Company of America (Citizens), THG s principal property and casualty companies; and certain other insurance and non-insurance subsidiaries. These legal entities conduct their operations through several business segments discussed in Note 11. All significant intercompany accounts and transactions have been eliminated. On January 2, 2009, the Company sold First Allmerica Financial Life Insurance Company (FAFLIC) to Commonwealth Annuity and Life Insurance Company (Commonwealth Annuity), a subsidiary of the Goldman Sachs Group, Inc. (Goldman Sachs). Results related to the sale of FAFLIC are reported as discontinued operations. Accounts associated with the accident and health insurance business that was retained by the Company have been classified as assets and liabilities of discontinued operations in the consolidated Balance Sheets (See Note 3 Discontinued Operations).

The accompanying interim consolidated financial statements reflect, in the opinion of the Company s management, all adjustments necessary for a fair presentation of the financial position and results of operations. The results of operations for the nine months ended September 30, 2010 are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the Company s 2009 Annual Report on Form 10-K filed with the Securities and Exchange Commission.

The preparation of financial statements in conformity with generally accepted accounting principles requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. New Accounting Pronouncements

Recently Implemented Standards

Accounting Standards Codification (ASC) 105, *Generally Accepted Accounting Principles* (ASC 105) reorganized by topic existing accounting and reporting guidance issued by the Financial Accounting Standards Board (FASB) into a single source of authoritative generally accepted accounting principles (GAAP) to be applied by nongovernmental entities. All guidance contained in the ASC carries an equal level of authority. Rules and interpretive releases of the Securities and Exchange Commission (SEC) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. Accordingly, all other accounting literature will be deemed non-authoritative . ASC 105 is effective on a prospective basis for financial statements issued for interim and annual periods ending after September 15, 2009. The Company has implemented the guidance included in ASC 105 as of July 1, 2009. The implementation of this guidance changed the Company s references to GAAP authoritative guidance but did not impact the Company s financial position or results of operations.

As of April 1, 2009, the Company adopted the guidance included in ASC 320, *Investments - Debt and Equity Securities* (ASC 320), which modifies the assessment of other-than-temporary impairments (OTTI) for fixed maturity securities, as well as the method of recording and reporting OTTI. Under the new guidance, if a company intends to sell or more likely than not will be required to sell a fixed maturity security before recovery of its amortized cost basis, the amortized cost of the security is reduced to its fair value, with a corresponding charge to earnings. If a company does not intend to sell the fixed maturity security, or more likely than not will not be required to sell it, the company is required to separate the other-than-temporary impairment into the portion which represents the credit loss and the amount related to all other factors. The amount of the estimated loss attributable to credit is recognized in earnings and the amount related to non-credit factors is recognized in accumulated other comprehensive income, net of applicable taxes. A cumulative effect adjustment was recognized by the Company upon adoption of this guidance to reclassify the non-credit component of previously recognized impairments from retained earnings to accumulated other comprehensive income. The Company increased the amortized cost basis of these fixed maturity securities and recorded a cumulative effect adjustment of $33.3 million as an increase to retained earnings and reduction to accumulated other comprehensive income. (See further disclosure in Note 8 Investments).

ASC 805, *Business Combinations* (ASC 805) contains guidance which was intended to provide additional clarification of application issues regarding initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. ASC 805 was effective for business combinations initiated on or after

9

the first annual reporting period beginning after December 15, 2008. The Company implemented this guidance effective January 1, 2009. Implementing this guidance did not have an effect on the Company s financial position or results of operations; however, it will likely have an impact on the Company s accounting for future business combinations, but the effect is dependent upon acquisitions, if any, that are made in the future.

In December 2009, the FASB issued ASC Update 2009-17, *Consolidation* (Topic 810) *Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities* (ASC Update 2009-17) which codified Statement of Financial Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)*. This guidance amends FASB Interpretation No. 46R, *Consolidation of Variable Interest Entities an interpretation of ARB No. 51* to require an analysis to determine whether a company has a controlling financial interest in a variable interest entity. This analysis identifies the primary beneficiary of a variable interest entity as the enterprise that has a) the power to direct the activities of a variable interest entity that most significantly impact the entity s economic performance and b) the obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. The statement requires an ongoing assessment of whether a company is the primary beneficiary of a variable interest entity when the holders of the entity, as a group, lose power, through voting or similar rights, to direct the actions that most significantly affect the entity s economic performance. This statement also enhances disclosures about a company s involvement in variable interest entities. ASC Update 2009-17 is effective as of the beginning of the first annual reporting period that begins after November 15, 2009. The Company implemented this guidance as of January 1, 2010. The effect of implementing this guidance was not material to the Company s financial position or results of operations.

ASC 820, *Fair Value Measurements and Disclosures* (ASC 820) includes guidance that was issued by the FASB which is to be considered when determining whether or not a transaction is orderly and clarifies the valuation of securities in markets that are not active. This guidance includes information related to a company s use of judgment, in addition to market information, in certain circumstances to value assets which have inactive markets. This fair value guidance in ASC 820 was effective for interim and annual reporting periods ending after June 15, 2009.

In August 2009, the FASB issued ASC Update No. 2009-05, *Fair Value Measurements and Disclosures (Topic 820): Measuring Liabilities at Fair Value*. This update amends ASC 820, *Fair Value Measurements and Disclosures* and provides further guidance on measuring the fair value of a liability. The guidance establishes the types of valuation techniques to be used to value a liability when a quoted market price in an active market for the identical liability is not available, such as the use of an identical or similar liability when traded as an asset. The guidance also further clarifies that a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are both Level 1 fair value measurements. If adjustments are required to be applied to the quoted price, it results in a level 2 or 3 fair value measurement. The guidance provided in the update is effective for the first reporting period (including interim periods) beginning after issuance.

In September 2009, the FASB issued ASC Update No. 2009-12, *Fair Value Measurements and Disclosures (Topic* 820): *Investments in Certain Entities that Calculate Net Asset Value per Share* (or Its Equivalent) (ASC Update No. 2009-12). This update sets forth guidance on using the net asset value per share provided by an investee to estimate the fair value of an alternative investment. Specifically, the update permits a reporting entity to measure the fair value of this type of investment on the basis of the net asset value per share of the investment (or its equivalent) if all or substantially all of the underlying investments used in the calculation of the net asset value is consistent with ASC 820. The update also requires additional disclosures by each major category of investment, including, but not limited to, fair value of underlying investments in the major category, significant investment strategies, redemption restrictions, and unfunded commitments related to investments in the major category. The amendments in this update are effective for interim and annual periods ending after December 15, 2009.

In January 2010, the FASB issued ASC Update 2010-06 (Topic 820) *Improving Disclosures about Fair Value Measurements* (ASC Update 2010-06). This update amends ASC 820 and requires new and clarified disclosures for fair value measurements. The guidance requires that transfers in and out of Levels 1 and 2 be disclosed separately, including a description of the reasons for such transfers. Additionally, the reconciliation of fair value measurements of Level 3 assets should separately disclose information about purchases, sales, issuance and settlements in a gross, rather than net disclosure presentation. The guidance further clarifies that fair value disclosures should be separately presented for each class of assets and liabilities and disclosures should be provided for valuation techniques and inputs for both recurring and non-recurring fair value measurements related to Level 2 and Level 3 categories. The disclosure guidance provided in the update is effective for reporting periods beginning after December 15, 2009. The Company implemented this guidance effective at January 1, 2010. Implementing this guidance did not have an effect on the Company s financial position or results of operations.

The Company applied the provisions of ASC 820 to its financial assets and liabilities upon adoption at January 1, 2008 and adopted the remaining provisions relating to certain nonfinancial assets and liabilities on January 1, 2009. The difference between the carrying amounts and fair values of those financial instruments held upon initial adoption, on January 1, 2008, was recognized as a cumulative effect adjustment to the opening balance of retained earnings and was not material to the Company s financial position or results of operations. The Company implemented the guidance related to orderly transactions under current market conditions as of April 1, 2009, which also was not material to the Company s financial position or results of operations. Furthermore, the implementation as of October 1, 2009 of ASC Update No. 2009-05 and ASC Update No. 2009-12 did not have a material effect on the Company s financial position or results of operations. (See further disclosure in Note 9 Fair Value).

ASC 855, *Subsequent Events* (ASC 855), and as modified by ASC update 2010-9, *Amendments to Certain Recognition and Disclosure Requirements*, includes guidance that was issued by the FASB in May 2009, and is consistent with current auditing standards in defining a subsequent event. Additionally, the guidance provides for disclosure regarding the existence of a company s evaluation of its subsequent events. ASC 855 defines two types of subsequent events, recognized and non-recognized . Recognized subsequent events provide additional evidence about conditions that existed at the date of the balance sheet and are required to be reflected in the financial statements. Non-recognized subsequent events provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date and, therefore, are not required to be reflected in the financial statements. However, certain non-recognized subsequent events may require disclosure to prevent the financial statements from being misleading. This guidance was effective prospectively for interim or annual financial periods ending after June 15, 2009. The Company implemented the guidance included in ASC 855 as of April 1, 2009 and the updated guidance as of December 31, 2009. The effect of implementing the guidance was not material to the Company s financial position or results of operations.

In December 2009, the FASB issued ASC Update 2009-16 *Transfers and Servicing* (Topic 860) - *Accounting for Transfers of Financial Assets* (ASC Update 2009-16) which codified Statement of Financial Accounting Standards No. 166, *Accounting for Transfers of Financial Assets an amendment of FASB Statement No. 140*. This guidance revises FASB Statement of Financial Accounting Standards No. 140, *Accounting for Transfers and Extinguishment of Liabilities a replacement of FASB Statement 125* and requires additional disclosures about transfers of financial assets, including securitization transactions, and any continuing exposure to the risks related to transferred financial assets. It also eliminates the concept of a qualifying special-purpose entity , changes the requirements for derecognizing financial assets, and enhances disclosure requirements. ASC Update 2009-16 is effective prospectively, for annual periods beginning after November 15, 2009, and interim and annual periods thereafter. The Company has implemented this guidance as of January 1, 2010. The effect of implementing this guidance was not material to the Company s financial position or results of operations.

Recently Issued Standards

In October 2010, the FASB issued ASC Update 2010-26 (Topic 944) *Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts (a consensus of the FASB Emerging Issues Task Force)*. This update provides clarity in defining which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral, commonly known as deferred acquisition costs. Additionally, this update specifies that only costs associated with the successful acquisition of a policy or contract may be deferred, whereas current industry practice often includes costs relating to unsuccessful contract acquisitions. This ASC Update is effective for fiscal years beginning after December 15, 2011. The Company is currently assessing the impact of this guidance to its financial position and results of operations.

3. Discontinued Operations

Discontinued operations primarily consist of: (i) FAFLIC s discontinued operations, including both the loss associated with the sale of FAFLIC on January 2, 2009 and the loss or income resulting from its prior business operations; (ii) losses or gains associated with the sale of the variable life insurance and annuity business in 2005; and (iii) the discontinued accident and health insurance business.

The following table summarizes the results for this discontinued business for the periods indicated:

	(Unaudited)	**(Unaudited)**
	Quarter Ended	**Nine months Ended September 30,**

	September 30,			
(In millions)	**2010**	2009	**2010**	2009
Gain from operations of discontinued FAFLIC business, net of taxes	**$ 0.5**	$ 0.4	**$ 0.4**	$ 6.3
Gain on disposal of variable life and annuity business, net of taxes	**$ 0.1**	$ -	**$ 1.0**	$ 4.1
Gain (loss) from discontinued accident and health insurance business, net of taxes	**$ 0.2**	$ 0.7	**$ (0.9)**	$ (2.4)
Other discontinued operations, net of taxes	**$ 0.1**	$ -	**$ 0.1**	$ -

Table of Contents

FAFLIC Discontinued Operations

On January 2, 2009, THG sold its remaining life insurance subsidiary, FAFLIC, to Commonwealth Annuity, a subsidiary of Goldman Sachs. Approval was obtained from the Massachusetts Division of Insurance for a pre-close dividend from FAFLIC consisting of designated assets with a statutory book value of approximately $130 million. Total proceeds from the sale, including the dividend, were approximately $230 million, net of transaction costs. Additionally, coincident with the sale transaction, Hanover Insurance and FAFLIC entered into a reinsurance contract whereby Hanover Insurance assumed FAFLIC s discontinued accident and health insurance business. THG has also indemnified Commonwealth Annuity for certain litigation, regulatory matters and other liabilities related to the pre-closing activities of the business transferred. The Company recognized, in 2008, a $77.3 million loss associated with this transaction.

The gain from FAFLIC s discontinued operations was $0.5 million and $0.4 million, net of tax, for the quarter and $0.4 million and $6.3 million, net of tax, for the nine months ended September 30, 2010 and 2009, respectively, and resulted primarily from a change in the Company s estimate of indemnification liabilities related to the sale.

As of September 30, 2010, the Company s total gross indemnification liability provided in connection with the sale of FAFLIC was $1.2 million. The Company regularly reviews and updates this liability for legal and regulatory matter indemnities. Although the Company believes its current estimate for this liability is appropriate, there can be no assurance that these estimates will not materially increase in the future. Adjustments to this reserve are recorded in the results of the Company in the period in which they are determined.

Variable Life Insurance and Annuity Business

On December 30, 2005, the Company sold its run-off variable life insurance and annuity business to Goldman Sachs, including the reinsurance of 100% of the variable business of FAFLIC. The Company agreed to indemnify Goldman Sachs for certain litigation, regulatory matters and other liabilities relating to the pre-closing activities of the business that was sold. In the third quarter of 2010, the Company recorded gains of $0.1 million, net of tax, and in the first nine months of 2010 and 2009, respectively, the Company recorded gains of $1.0 million and $4.1 million, net of tax, primarily due to a change in the Company s estimate of indemnification liabilities.

As of September 30, 2010, the Company s total gross liability for guarantees and indemnifications provided in connection with the disposal of its variable life insurance and annuity business was $4.1 million. The Company regularly reviews and updates this liability for legal and regulatory matter indemnities. Although the Company believes its current estimate for this liability is appropriate, there can be no assurance that these estimates will not materially increase in the future. Adjustments to this reserve are recorded in the results of the Company in the period in which they are determined.

Accident and Health Insurance Business

During 1999, the Company exited its accident and health insurance business, consisting of its Employee Benefit Services business, its Affinity Group Underwriters business and its accident and health assumed reinsurance pool business. Prior to 1999, these businesses comprised substantially all of the former Corporate Risk Management Services segment. Accordingly, the operating results of the discontinued segment have been reported in accordance with Accounting Principles Board Opinion No. 30, *Reporting the Results of Operations Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions* (APB Opinion No. 30). On January 2, 2009, Hanover Insurance directly assumed a portion of the accident and health insurance business; and therefore continues to apply APB Opinion No. 30 to this business. In addition, the remainder of the FAFLIC accident and health business was reinsured by Hanover Insurance and has been reported in accordance with ASC 205.

During the quarters ended September 30, 2010 and 2009, the Company recognized gains of $0.2 million and $0.7 million, net of tax, respectively, from its discontinued accident and health insurance business. For the nine months ended September 30, 2010 and 2009, the Company recognized losses of $0.9 million and $2.4 million, net of tax, related to this business. Losses for the nine months ended September 30, 2010 were driven by increased reserves resulting from the Company s current interpretation of the provisions of the Patient Protection and Affordable Care Act, as well as realized investment losses due to impairments. These were partially offset by net investment income. Losses for the nine months ended September 30, 2009 primarily reflect realized investment losses due to impairments.

Table of Contents

At September 30, 2010 and December 31, 2009, the portion of the discontinued accident and health insurance business that was directly assumed had assets of $58.9 million and $54.0 million, respectively, consisting primarily of invested assets, and liabilities of approximately $53.3 million and $48.7 million, respectively, consisting primarily of policy liabilities. At September 30, 2010 and December 31, 2009, the assets and liabilities of this business, as well as those of the reinsured portion of the accident and health insurance business are classified as assets and liabilities of discontinued operations in the Consolidated Balance Sheets.

4. Other Significant Transactions

On September 23, 2010, June 7, 2010 and March 22, 2010, the Company paid dividends of 25 cents per share to its issued and outstanding common stock shareholders of record at the close of business on September 10, 2010, May 24, 2010 and March 8, 2010, respectively. The total dividends paid in the quarters ended September 30, 2010, June 30, 2010 and March 31, 2010 were $11.6 million, $12.0 million and $12.3 million, respectively. On an annualized basis, these dividend payments represent a 33% increase over the annual dividend of 75 cents, paid in December 2009. The holding company receives dividends from its insurance subsidiaries; such dividends are restricted through state regulation. Both Citizens and Hanover Insurance paid dividends to their parent companies in 2009. Citizens could not pay a dividend to Hanover Insurance without the prior approval of the state regulators until June 2010. Beginning in June 2010, Citizens was able to pay up to $70.3 million without the prior approval of state regulators. In September 2010, Citizens declared a $70 million dividend to Hanover Insurance. Hanover Insurance cannot pay a dividend to the holding company without the prior approval of the state regulators until December 2010. In December 2010, the maximum dividend that Hanover Insurance can pay without the prior approval of state regulators will be $173.7 million.

On June 14, 2010, the Company purchased approximately 11 acres of developable land in Worcester, Massachusetts for $5 million. A portion of the land will be developed with the construction of a new 200,000 square foot office building and the redevelopment of an adjacent parking garage. In addition, the Company signed a 17 year lease agreement with a tenant for the new building and garage. The tenant is an unaffiliated public company with an investment grade credit rating. Through September 30, 2010, the Company capitalized $6.8 million in related lease acquisition, legal, architectural and associated costs. Development costs are estimated between $65 million and $70 million and the project will be financed, in part, through the issuance of collateralized debt through the Company s membership in the Federal Home Loan Bank of Boston (FHLBB). In July 2010, Hanover Insurance committed to borrow $46.3 million from the FHLBB to finance the project. These borrowings will be drawn in several increments from July 2010 to January 2012. On July 19, 2010, Hanover Insurance received an advance of $7.6 million from this commitment. Amounts drawn from the $46.3 million mature on July 20, 2020 and carry fixed interest rates with a weighted average of 3.88%. (See also below for further information related to participation in the FHLBB s collateralized borrowing program).

On March 31, 2010, the Company acquired Campania for a cash purchase price of approximately $24 million, subject to various terms and conditions. Campania specializes in insurance solutions for portions of the healthcare industry.

Through October 2010, the Company s Board of Directors has authorized aggregate repurchases of the Company s common stock of up to $500 million, including a recent $100 million increase in the program. Under the repurchase authorizations, the Company may repurchase its common stock from time to time, in amounts and prices and at such times as deemed appropriate, subject to market conditions and other considerations. The Company s repurchases may be executed using open market purchases, privately negotiated transactions, accelerated repurchase programs or other transactions. The Company is not required to purchase any specific number of shares or to make purchases by any certain date under this program. On March 30, 2010 and December 8, 2009, the Company entered into accelerated share repurchase agreements with Barclays Bank PLC, acting through its agent Barclays Capital, Inc., for the immediate repurchase of 2.3 million and 2.4 million shares, respectively, of the Company s common stock at a cost of approximately $100.9 million and $100.6 million, respectively (in each case, subject to adjustment). The Company settled its accelerated stock repurchase program initiated in December 2009 on June 23, 2010 for an additional payment of $4.6 million provided to Barclays Bank PLC. Total repurchases under these programs as of September 30, 2010 were 7.9 million shares at a cost of $338.8 million.

On February 23, 2010, the Company issued $200.0 million aggregate principal amount of 7.50% senior unsecured notes due March 1, 2020. The senior debentures are subject to certain restrictive covenants, including limitations on the issuance or disposition of capital stock of restricted subsidiaries and limitations on liens. These debentures pay interest semi-annually on March 1 and September 1.

On December 3, 2009, the Company entered into a renewal rights agreement with OneBeacon Insurance Group, LTD. (OneBeacon). Through this agreement, the Company acquired access to a portion of OneBeacon s small and middle market commercial business at renewal, including industry programs and middle market niches. This transaction included consideration of approximately $23 million, plus certain potential additional consideration, primarily representing purchased renewal rights intangible assets which are included as Other Assets in the Consolidated Balance Sheets. The agreement was effective for renewals beginning January 1, 2010.

Table of Contents

On September 25, 2009, Hanover Insurance received an advance of $125 million through its membership in the FHLBB as part of a collateralized borrowing program. This advance bears interest at a fixed rate of 5.50% per annum over a twenty-year term. The proceeds from the borrowing were used by Hanover Insurance to acquire AIX and its subsidiaries from the holding company. As noted above, in July 2010 an additional $7.6 million advance was received from the FHLBB. As collateral to the FHLBB for all advances received as of September 30, 2010, Hanover Insurance has pledged government agency securities with a fair value of $153.7 million. Collateral pledged to the FHLBB totaled $142.0 million as of December 31, 2009. The fair value of the collateral pledged must be maintained at certain specified levels of the borrowed amount, which can vary depending on the type of assets pledged. If the fair value of this collateral declines below these specified levels, Hanover Insurance would be required to pledge additional collateral or repay outstanding borrowings. Hanover Insurance is permitted to voluntarily repay the outstanding borrowings at any time, subject to a repayment fee. As a requirement of membership in the FHLBB, Hanover Insurance acquired $2.5 million of FHLBB stock, and as a condition to participating in the FHLBB s collateralized borrowing program, it was required to purchase additional shares of FHLBB stock in an amount equal to 4.5% of its outstanding borrowings. Such purchases totaled $6.0 million through September 30, 2010.

The Company liquidated AFC Capital Trust I (the Trust) on July 30, 2009. Each holder of 8.207% Series B Capital Securities (Capital Securities) as of that date received a principal amount of the Company s Series B 8.207% Junior Subordinated Deferrable Interest Debentures (Junior Debentures) due February 3, 2027 equal to the liquidation amount of the Capital Securities held by such holder. The liquidation of the Trust did not have a material effect on the Company s results of operations or financial position.

On June 29, 2009, prior to liquidating the Trust, the Company completed a cash tender offer to repurchase a portion of its Capital Securities that were issued by the Trust and a portion of its 7.625% Senior Debentures (Senior Debentures) due in 2025 that were issued by THG. As of that date, $69.3 million of Capital Securities were tendered at a price equal to $800 per $1,000 of face value. In addition, the Company accepted for tender a principal amount of $77.3 million of Senior Debentures. Depending on the time of tender, holders of the Senior Debentures accepted for purchase received a price of either $870 or $900 per $1,000 of face value. Separately, the Company held $65.0 million of Capital Securities previously repurchased at a discount in the open market prior to the tender offer, and $1.1 million of Senior Debentures. The Company recognized a pre-tax gain of $34.5 million in 2009 as a result of such purchases. During the first quarter of 2010, the Company repurchased $0.4 million of Junior Debentures at a slight gain. As of September 30, 2010, a net principal amount of $165.3 million of their Junior Debentures and $121.4 million of their Senior Debentures, which are not held by us, remained outstanding.

5. Debt

Long-term debt consists of the following:

	(Unaudited)	
(In millions)	**September 30, 2010**	**December 31, 2009**
Senior debentures (unsecured) maturing March 1, 2020	**$ 199.3**	$ -
Senior debentures (unsecured) maturing October 16, 2025	**121.4**	121.4
Holding Company junior subordinated debentures	**165.3**	165.7
FHLBB borrowing	**132.6**	125.0
Capital securities	**17.4**	17.8
Surplus notes	**4.0**	4.0
	$ 640.0	$ 433.9

On February 23, 2010, the Company issued $200 million aggregate principal amount of 7.50% senior unsecured notes due March 1, 2020. The senior debentures are subject to certain restrictive covenants, including limitations on the issuance or disposition of capital stock of restricted subsidiaries and limitations on liens. These debentures pay interest semi-annually (See also Note 4 Other Significant Transactions). The Company is in compliance with the covenants associated with this indenture.

The Company also holds senior unsecured notes issued with a face value of $200.0 million on October 16, 1995. In 2009, the Company repurchased a portion of these senior debentures with a face value of $78.4 million. The remaining senior debentures have a $121.4 million face value, pay interest semi-annually at a rate of 7.625% and mature on October 16, 2025. The senior debentures are subject to certain restrictive covenants, including limitations on the issuance or disposition of stock of restricted subsidiaries and limitations on liens (See also Note 4 Other Significant Transactions). The Company is in compliance with the covenants associated with this indenture.

AFC Capital Trust I issued $300.0 million of preferred securities in 1997, the proceeds of which were used to purchase junior subordinated debentures issued by the Company. The Company liquidated the Trust on July 30, 2009. Each holder of Capital Securities as of that date received a principal amount of the Company s Series B Junior Subordinated Deferrable Interest Debentures equal to the liquidation amount of the Capital Securities held by such holder. In 2010 and 2009, the Company repurchased a portion of these debentures with a face value of $0.4 million and $134.3 million, respectively. These junior subordinated debentures have a face value of $165.3 million and $165.7 million as of September 30, 2010 and December 31, 2009, respectively, and consistent with the capital securities, pay cumulative dividends semi-annually at 8.207% and mature February 3, 2027 (See also Note 4 Other Significant Transactions). These securities are subject to certain restrictive covenants, with which the Company is in compliance. In addition, the Company holds $3.0 million of capital securities related to Professionals Direct, Inc., and $14.4 million of capital securities related to AIX Holdings, Inc. as of September 30, 2010.

In September 2009, Hanover Insurance received an advance of $125.0 million through its membership in the FHLBB as part of a collateralized borrowing program (FHLBB 2009). This advance bears interest at a fixed rate of 5.50% per annum over a twenty-year term. In July 2010, the Company committed to borrow an additional $46.3 million from FHLBB to finance the development of City Square. These borrowings will be drawn in several increments from July 2010 to January 2012. All amounts mature on July 20, 2020 and carry fixed interest rates with a weighted average of 3.88%. Through September 30, 2010, the Company has borrowed $7.6 million under this arrangement (FHLBB 2010). All interest associated with this additional $46.3 million will be capitalized through the construction phase of the City Square project. As collateral to FHLBB, Hanover Insurance has pledged government agency securities with a fair value of $153.7 million and $142.0 million as of September 30, 2010 and December 31, 2009, respectively (See also Note 4 Other Significant Transactions). The Company is in compliance with the covenants associated with these borrowings.

In June 2007, the Company entered into a $150.0 million committed syndicated credit agreement which expired in June 2010. There were no borrowings under this agreement. The agreement provided covenants, including, but not limited to, maintaining a certain level of equity and an RBC ratio in the Company s primary property and casualty companies of at least 175% (based on the Industry Scale). The Company was in compliance with the covenants of this agreement for the duration of the contract. The Company did not renew or replace this syndicated credit agreement upon expiration. Additionally, the Company had no commercial paper borrowings as of September 30, 2010 and the Company does not anticipate utilizing commercial paper in the near term.

Interest expense was $32.8 million for the nine months ended September 30, 2010 and $27.2 million for the nine months ended September 30, 2009 and included interest related to the Company s senior debentures, junior subordinated debentures, FHLBB borrowings, capital securities and surplus notes. All interest expense is recorded in other operating expenses.

6. Federal Income Taxes

Federal income tax expense for the nine months ended September 30, 2010 and 2009 has been computed using estimated effective tax rates. These rates are revised, if necessary, at the end of each successive interim period to reflect current estimates of the annual effective tax rates.

The Company or its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. With few exceptions, the Company and its subsidiaries are no longer subject to U.S. federal income tax examinations by tax authorities for years before 2005. In September 2009, the Company received a Revenue Agents Report for the 2005 and 2006 IRS audit. The Company has agreed to all proposed adjustments other than a disallowance of Separate Account Dividends Received Deductions for which the Company has requested an Appeals conference. Due to available net operating loss carryovers and the 2005 sale of Allmerica Financial Life Insurance and Annuity Company, the effects of the proposed adjustments do not materially affect the Company s financial position. The IRS audits of the years 2007 and 2008 commenced in April 2010. The Company and its subsidiaries are still subject to U.S. state income tax examinations by tax authorities for years after 1998.

7. Pension and Other Postretirement Benefit Plans

The Company s defined benefit pension plans, which provided retirement benefits based on a cash balance formula, were frozen as of January 1, 2005; therefore, no further cash balance allocations have been credited for plan years beginning on or after January 1, 2005. In addition, certain transition group employees were eligible for a grandfathered benefit based upon service and compensation; such benefits were also frozen at January 1, 2005 levels with an annual transition pension adjustment. The Company has additional unfunded pension plans and postretirement plans to provide benefits to certain full-time employees, former FAFLIC agents, retirees and their dependents.

15

Table of Contents

The components of net periodic benefit cost for pension and other postretirement benefit plans are as follows:

	(Unaudited)			
	Quarter Ended September 30,			
(In millions)	**2010**	**2009**	**2010**	**2009**
	Pension Benefits		Postretirement Benefits	
Service cost benefits earned during the period	**$ 0.1**	$ 0.1	**$ -**	$ -
Interest cost	**8.2**	8.4	**0.7**	0.7
Expected return on plan assets	**(8.8)**	(6.4)	**-**	-
Recognized net actuarial loss	**4.2**	6.7	**0.1**	0.1
Amortization of transition asset	**(0.4)**	(0.4)	**-**	-
Amortization of prior service cost	**-**	-	**(1.5)**	(1.4)
Net periodic cost (benefit)	**$ 3.3**	$ 8.4	**$ (0.7)**	$ (0.6)

	(Unaudited)			
	Nine months Ended September 30,			
	2010	**2009**	**2010**	**2009**
	Pension Benefits		Postretirement Benefits	
Service cost benefits earned during the period	**$ 0.1**	$ 0.1	**$ 0.1**	$ 0.1
Interest cost	**24.5**	25.4	**2.0**	2.1
Expected return on plan assets	**(26.3)**	(19.1)	**-**	-
Recognized net actuarial loss	**12.6**	20.2	**0.3**	0.2
Amortization of transition asset	**(1.2)**	(1.2)	**-**	-
Amortization of prior service cost	**-**	-	**(4.4)**	(4.3)
Net periodic cost (benefit)	**$ 9.7**	$ 25.4	**$ (2.0)**	$ (1.9)

On January 4, 2010, the Company made a discretionary contribution of $100.0 million to the qualified defined benefit pension plan. With this contribution, and based upon the current estimate of liabilities and certain assumptions regarding investment return and other factors, the Company s qualified defined benefit pension plan is essentially fully funded.

Table of Contents

8. Investments

A. Fixed maturities and equity securities

The Company holds investments in fixed maturities and equity securities, which are classified as available for sale, in accordance with ASC 320, *Investments Debt and Equity Securities*.

The amortized cost and fair value of available-for-sale fixed maturities and equity securities were as follows:

(Unaudited)

(In millions)	September 30, 2010				
			Gross Unrealized Losses		
	Amortized Cost (1)	Gross Unrealized Gains	Unrealized Losses	OTTI Unrealized Losses (2)	Fair Value
U.S. Treasury securities and U.S. government and agency securities	**$ 232.4**	**$ 8.3**	**$ 0.5**	**$ -**	**$ 240.2**
States and political subdivisions	**931.9**	**48.1**	**7.6**	**-**	**972.4**
Foreign governments	**3.0**	**-**	**-**	**-**	**3.0**
Corporate fixed maturities	**2,404.8**	**239.8**	**3.2**	**25.5**	**2,615.9**
Residential mortgage-backed securities	**787.0**	**48.5**	**0.7**	**8.4**	**826.4**
Commercial mortgage-backed securities	**346.2**	**21.3**	**1.2**	**-**	**366.3**
Total fixed maturities, including assets of discontinued operations	**4,705.3**	**366.0**	**13.2**	**33.9**	**5,024.2**
Less: fixed maturities of discontinued operations	**(116.5)**	**(9.1)**	**(0.2)**	**(5.8)**	**(119.6)**
Total fixed maturities, excluding discontinued operations	**$ 4,588.8**	**$ 356.9**	**$ 13.0**	**$ 28.1**	**$ 4,904.6**
Equity securities, excluding discontinued operations	**$ 112.3**	**$ 13.7**	**$ 0.3**	**$ -**	**$ 125.7**

(In millions)	December 31, 2009				
			Gross Unrealized Losses		
	Amortized Cost (1)	Gross Unrealized Gains	Unrealized Losses	OTTI Unrealized Losses (2)	Fair Value
U.S. Treasury securities and U.S. government and agency securities	$ 355.2	$ 3.2	$ 3.7	$ -	$ 354.7
States and political subdivisions	844.7	13.1	25.6	-	832.2
Foreign governments	3.0	-	-	-	3.0
Corporate fixed maturities	2,243.7	131.4	14.3	29.9	2,330.9
Residential mortgage-backed securities	858.8	29.7	3.4	10.7	874.4
Commercial mortgage-backed securities	334.5	10.1	7.4	-	337.2
Total fixed maturities, including assets of discontinued operations	4,639.9	187.5	54.4	40.6	4,732.4

Less: fixed maturities of discontinued operations	(119.6)	(6.0)	(2.0)	(6.8)	(116.8)
Total fixed maturities, excluding discontinued operations	$ 4,520.3	$ 181.5	$ 52.4	$ 33.8	$4,615.6
Equity securities, excluding discontinued operations	$ 57.3	$ 12.2	$ 0.3	$ -	$ 69.2

(1) Amortized cost for fixed maturities and cost for equity securities.

(2) Represents other-than-temporary impairments recognized in accumulated other comprehensive income. Amount excludes net unrealized gains on impaired securities relating to changes in the value of such securities subsequent to the impairment measurement date of $39.2 million and $30.1 million as of September 30, 2010 and December 31, 2009, respectively.

The amortized cost and fair value by maturity periods for fixed maturities are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties, or the Company may have the right to put or sell the obligations back to the issuers. Mortgage-backed securities are included in the category representing their stated maturity.

	(Unaudited)	
(In millions)	September 30, 2010	
	Amortized Cost	Fair Value
Due in one year or less	$182.9	$ 185.9
Due after one year through five years	1,218.8	1,309.3
Due after five years through ten years	1,570.5	1,716.2
Due after ten years	1,733.1	1,812.8
Total fixed maturities, including assets of discontinued operations	4,705.3	5,024.2
Less: fixed maturities of discontinued operations	(116.5)	(119.6)
Total fixed maturities, excluding assets of discontinued operations	$ 4,588.8	$ 4,904.6

B. Securities in an unrealized loss position

The following tables provide information about the Company s fixed maturities and equity securities that are in an unrealized loss position at September 30, 2010 and December 31, 2009:

	(Unaudited)					
	September 30, 2010					
	12 months or less		Greater than 12 months		Total	
(In millions)	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI (1)	Fair Value
Fixed maturities:						
Investment grade:						
U.S. Treasury securities and U.S. government and agency securities	$ -	$ 11.1	$ 0.5	$ -	$ 0.5	$ 11.1
States and political subdivisions	2.1	29.7	5.5	94.3	7.6	124.0
Corporate fixed maturities	0.3	13.7	12.3	96.9	12.6	110.6
Residential mortgage-backed securities	0.1	35.8	9.0	33.0	9.1	68.8
Commercial mortgage-backed securities	-	5.8	1.2	8.1	1.2	13.9

Total investment grade	**2.5**	**96.1**	**28.5**	**232.3**	**31.0**	**328.4**
Below investment grade (2):						
Corporate fixed maturities	**0.7**	**20.4**	**15.4**	**124.9**	**16.1**	**145.3**
Total fixed maturities	**3.2**	**116.5**	**43.9**	**357.2**	**47.1**	**473.7**
Equity securities:						
Common equity securities	**0.3**	**11.4**	**-**	**-**	**0.3**	**11.4**
Total (3)	**$ 3.5**	**$ 127.9**	**$ 43.9**	**$ 357.2**	**$ 47.4**	**$ 485.1**

(1) Includes $33.9 million unrealized loss related to other-than-temporary impairment losses recognized in other comprehensive income, of which $15.1 million are below investment grade aged greater than 12 months.
(2) Substantially all below investment grade securities with an unrealized loss had been rated by the NAIC, Standard & Poor s or Moody s at September 30, 2010.
(3) Includes discontinued accident and health insurance business of $6.0 million in total gross unrealized losses with $40.5 million in fair value at September 30, 2010.

Table of Contents

	December 31, 2009					
	12 months or less		Greater than 12 months		Total	
(In millions)	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI	Fair Value	Gross Unrealized Losses and OTTI (1)	Fair Value
Fixed maturities:						
Investment grade:						
U.S. Treasury securities and U.S. government and agency securities	$ 3.7	$ 170.8	$ -	$ -	$ 3.7	$ 170.8
States and political subdivisions	9.0	275.2	15.6	176.5	24.6	451.7
Corporate fixed maturities	3.4	115.8	13.3	152.7	16.7	268.5
Residential mortgage-backed securities	6.6	89.1	7.5	62.6	14.1	151.7
Commercial mortgage-backed securities	0.4	13.5	7.0	30.0	7.4	43.5
Total investment grade	23.1	664.4	43.4	421.8	66.5	1,086.2
Below investment grade (2):						
States and political subdivisions	0.2	8.7	0.8	8.2	1.0	16.9
Corporate fixed maturities	10.6	84.1	16.9	150.1	27.5	234.2
Total below investment grade	10.8	92.8	17.7	158.3	28.5	251.1
Total fixed maturities	33.9	757.2	61.1	580.1	95.0	1,337.3
Equity securities:						
Common equity securities	-	-	0.3	1.4	0.3	1.4
Total (3)	$ 33.9	$ 757.2	$ 61.4	$ 581.5	$ 95.3	$ 1,338.7

(1) Includes $40.6 million unrealized loss related to other-than-temporary impairment losses recognized in other comprehensive income, of which $14.8 million are below investment grade aged greater than 12 months.
(2) Substantially all below investment grade securities with an unrealized loss had been rated by the NAIC, Standard & Poor s or Moody s at December 31, 2009.
(3) Includes discontinued accident and health insurance business of $8.8 million in total gross unrealized losses with $55.0 million in fair value at December 31, 2009.

The Company employs a systematic methodology to evaluate declines in fair value below amortized cost for all investments. The methodology utilizes a quantitative and qualitative process ensuring that available evidence concerning the declines in fair value below amortized cost is evaluated in a disciplined manner. In determining whether a decline in fair value below amortized cost is other-than-temporary, the Company evaluates several factors and circumstances, including the issuer s overall financial condition; the issuer s credit and financial strength ratings; the issuer s financial performance, including earnings trends, dividend payments and asset quality; any specific events which may influence the operations of the issuer; a weakening of the general market conditions in the industry or geographic region in which the issuer operates; the length of time and the degree to which the fair value of an issuer s securities remains below the Company s cost; with respect to fixed maturity investments, any factors that might raise doubt about the issuer s ability to pay all amounts due according to the contractual terms and whether the Company expects to recover the entire amortized cost basis of the security; and with respect to equity securities, the Company s ability and intent to hold the investment for a period of time to allow for a recovery in value. The Company applies these factors to all securities.

Table of Contents

The following tables provide information on the Company s gross unrealized losses of fixed maturity securities by credit ratings, including ratings of securities with third party guarantees, as of September 30, 2010 and December 31, 2009.

(Unaudited)

September 30, 2010

(In millions)	AAA	AA	A	BBB	Total investment grade	BB	B	CCC and below	Total below investment grade	Total
U.S. Treasury securities and U.S government and agency securities	$ 0.5	$ -	$ -	$ -	$ 0.5	$ -	$ -	$ -	$ -	$ 0.5
States and political subdivisions										