NeuroMetrix, Inc.
Form 10-K
March 14, 2008

Use these links to rapidly review the document

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2007

OR

o **TRANSITION REPORT PURSUANT TO SECTION 12 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to
Commission File Number 000-50856

NEUROMETRIX, INC.

(Exact name of registrant as specified in its charter)

Delaware	**04-3308180**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
62 Fourth Avenue Waltham, Massachusetts	**02451**
(Address of principal executive offices)	(Zip Code)

(781) 890-9989

(Registrant's telephone number, including area code)

Securities Registered Pursuant To Section 12(b) of the Act:

Title of each class	**Name of exchange on which registered**
Common Stock, $0.0001 par value per share	The NASDAQ Stock Market LLC
Preferred Stock Purchase Rights	

Securities Registered Pursuant to Section 12(g) of the Act

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes o No ý

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

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

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

Large accelerated filer o	Accelerated filer ý	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of June 30, 2007 the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $99,334,533 based on the closing sale price of the common stock as reported on the NASDAQ Global Market on June 30, 2007. For this computation, the registrant has excluded the market value of all outstanding shares beneficially owned by any director, executive officer or person known to the registrant to beneficially own 10% or more of the registrant's common stock; such exclusion shall not be deemed to constitute an admission that any such person is an affiliate of the registrant.

As of March 7, 2008, there were 13,690,134 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for the registrant's 2008 annual meeting of stockholders, which is expected to be filed pursuant to Regulation 14A within 120 days of the registrant's year ended December 31, 2007, are incorporated by reference into Part III of this Annual Report on Form 10-K.

NEUROMETRIX, INC.
ANNUAL REPORT ON FORM 10-K
YEAR ENDED DECEMBER 31, 2007

TABLE OF CONTENTS

PART I

The statements contained in this annual report on Form 10-K, including under the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and other sections of this annual report, include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including, without limitation, statements regarding our or our management's expectations, hopes, beliefs, intentions or strategies regarding the future. The words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect," "plan" and similar expressions may identify forward-looking statements, but the absence of these words does not mean that a statement is not forward-looking. The forward-looking statements contained in this annual report are based on our current expectations and beliefs concerning future developments and their potential effects on us. There can be no assurance that future developments affecting us will be those that we have anticipated. These forward-looking statements involve a number of risks, uncertainties (some of which are beyond our control) or other assumptions that may cause actual results or performance to be materially different from those expressed or implied by these forward-looking statements. These risks and uncertainties include, but are not limited to, those factors described in the section titled "Risk Factors." Should one or more of these risks or uncertainties materialize, or should any of our assumptions prove incorrect, actual results may vary in material respects from those projected in these forward-looking statements. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required under applicable securities laws.

ITEM 1: BUSINESS

Our Business An Overview

We design, develop and market proprietary medical devices used to help physicians diagnose and treat diseases of the nervous system such as neuropathies, which are disorders of the peripheral nerves and parts of the spine, and neurovascular disorders such as diabetic retinopathy. We are also developing medical devices designed to be used to provide regional anesthesia and pain control. To date, our focus has been on products that help physicians with the diagnosis or detection of neuropathies and neurovascular disorders. We have two product lines cleared by the United States Food and Drug Administration, or FDA, that are currently being marketed primarily to physicians and clinics, including the NC-stat System for the assessment of neuropathies and the DigiScope for the detection of eye disorders such as diabetic retinopathy.

Neuropathies are diseases of the peripheral nerves and parts of the spine that frequently are caused by or associated with diabetes, low back pain and carpal tunnel syndrome, or CTS, as well as other clinical disorders. We believe that our neuropathy diagnostic system, the NC-stat System, improves the quality and efficiency of patient care by offering all physicians the ability to diagnose patients with neuropathies at the point-of-service, that is, in the physician's office at the time the patient is examined, resulting in earlier and more accurate detection, greater patient comfort and convenience, and, in many cases, improved clinical and economic outcomes. The NC-stat System has been on the market since May 1999 and is used in over 5,500 physicians' offices and clinics in the United States. Over one million patients have had nerve conduction tests performed using the NC-stat System. We are currently developing a traditional nerve conduction system, the ADVANCE System, designed to help physicians with the diagnosis of neuropathies and have filed a 510(k) application with the FDA. The ADVANCE System is expected to provide physicians with even greater clinical functionality and is expected to be marketed to specialists such as neurologists as well as primary care physicians.

Neuropathies traditionally have been evaluated by simple clinical examination by the primary care physician, and, in some cases, subsequently diagnosed by a nerve conduction study and needle

electromyography, or NCS/nEMG, procedure performed by a neurologist or physician in a related specialty or their clinical staff. We estimate that there are approximately two million traditional NCS/nEMG procedures currently performed each year in the United States. We believe that use of traditional NCS/nEMG procedures is limited by: (1) the need to obtain a referral to a neurologist for the procedure and the resulting delay in availability of diagnostic information; (2) the inconvenience and discomfort of these procedures for the patient; and (3) the expense to the patient and third-party payer. We anticipate that the advantages and increased availability of a point-of-service product offering such as the NC-stat System could increase the number of nerve conduction studies performed. Based on our analysis of current data, we estimate that the potential market size for point-of-service nerve conduction studies in the diabetes, low back pain and CTS markets in the aggregate could be greater than 9.5 million annual patient tests, estimated to be more than $1.0 billion annually in the United States. We believe there is potentially a large market opportunity for our nerve conduction product line in the international markets and we recently launched the NC-stat System in the U.K. on a limited basis.

Diabetic retinopathy is a common neurovascular complication of diabetes and is the leading cause of blindness among working age adults. On December 26, 2007, we acquired substantially all of the assets and assumed certain liabilities of EyeTel Imaging, Inc., or EyeTel, whose product, the DigiScope, is a retinal imaging system designed for use at the point-of-service in primary diabetes care physician offices and optometry clinics for the detection of diabetic retinopathy and certain other eye disorders. Previously, we had obtained an exclusive sales and marketing license to the DigiScope from EyeTel for the primary diabetes care market. If abnormalities are detected using the DigiScope, the patient can then be referred to an ophthalmologist for treatment if deemed necessary. It is recommended by the American Diabetes Association, or ADA, that all patients with diabetes receive an annual dilated eye examination, which may be performed using the DigiScope, to determine if there are any abnormalities. There are approximately 21 million people in the United States with diabetes according to the ADA and only approximately 50% comply with the recommendation to have an annual eye examination. We believe that a product such as the DigiScope in primary diabetes care physician offices and optometry clinics could potentially lead to an increase in the level of testing and result in the earlier detection of eye disorders in patients with diabetes. Currently, there are approximately 190 physician practices and clinics in the United States using the DigiScope.

Our goal is to become the leading provider of innovative, proprietary, high gross margin medical devices that provide comprehensive solutions to help physicians with the diagnosis and treatment of patients with diseases of the nervous system, including neuropathies, and neurovascular disorders and provide solutions for regional anesthesia and pain control. We believe that our core technologies can be leveraged into additional diagnostic and therapeutic products.

One of the areas we are leveraging our core technology into is the minimally invasive delivery of commercially available drugs and other therapeutic agents using a proprietary delivery system for regional anesthesia, pain control and the treatment of neuropathies. We are currently in the clinical stage of development of a nerve localization system, which we refer to as NAVIGATOR, and expect to submit a 510(k) application to the FDA in the second half of 2008.

We are also pursuing product development efforts focused on neural repair and regeneration. We are in the early stages of developing a product for the treatment of peripheral nerve injuries by promoting nerve regeneration through electrical stimulation. We are pursuing these product development efforts through a joint venture established in February 2008 with Cyberkinetics Neurotechnology Systems, Inc., or Cyberkinetics, a medical device company focused on the treatment of neurological conditions. This product is in the preclinical stage of development. In November 2007, prior to the formation of the joint venture, we entered into a strategic alliance with Cyberkinetics through an investment of $2.5 million in shares of Cyberkinetics common stock. (See Strategic Alliance.)

We sell our products through a sales force of approximately fifty regional sales managers, five regional sales directors and a national sales director for sales of our products to physician offices and clinics.

Our revenues declined 19.2% to $44.6 million in 2007, after increasing 61.1% to $55.2 million in 2006 from $34.3 million in 2005. The decline in revenues was primarily attributable to challenges experienced with reimbursement of nerve conduction studies performed using the NC-stat System. The American Medical Association, or AMA, CPT Editorial Panel ("the CPT Panel") has been reviewing the reimbursement coding for nerve conduction studies and recently met in February 2008 to consider various proposals set forth by a work group formed by the CPT Panel. At this meeting, we believe that the CPT Panel approved a new Category III CPT Code for nerve conduction studies performed using equipment with certain automated features such as the NC-stat System. Unless we are able to successfully challenge this decision, a new Category III CPT Code would likely be published in July 2008 and become effective in January 2009. If the CPT Panel ultimately implements a Category III CPT code, this is likely to have a material and adverse impact on our business given that it is likely to result in limited or no Medicare reimbursement since there is the potential that no specified reimbursement values would be assigned to such codes and they do not automatically appear on the Medicare physician fee schedule. This could also adversely impact reimbursement by other third party payers and could have an adverse and material impact on our revenues and results of operations.

The majority of our revenues in 2007 were derived from sales of the NC-stat System and approximately 88% of our revenues were attributable to sales of the disposable biosensors that physicians use to perform nerve conduction tests with our NC-stat System. We recorded a net loss of $8.4 million in 2007 compared with net income of $4.3 million in 2006 and net income of $249,300 in 2005. Our net loss in 2007 was a result of the decline in revenues and an increase in operating expenses.

Neuropathies

Disorders of the nerves are broadly described by the term neuropathies. There are two basic types of neuropathies, those that are focal, or localized in nature, and those that are systemic. Focal neuropathies are typically caused by a compression of one or more specific nerves. Systemic neuropathies are typically caused by a metabolic disturbance that results in widespread damage to nerves throughout the body. The most common clinical conditions associated with neuropathies include:

Diabetes. Diabetes is a disease in which the body either does not produce sufficient quantities of insulin or does not properly use insulin. Insulin is a hormone that is needed to convert sugar, starches and other food into energy needed for daily body function. Diabetes often results in a high level of glucose in the blood, called hyperglycemia. Chronic hyperglycemia is associated with complications of diabetes including nerve, eye and kidney disease. The most common form of diabetes-related nerve disease is a systemic neuropathy called diabetic peripheral neuropathy, or DPN. The symptoms of DPN include impaired sensation or pain in the feet and hands. The ADA estimates that 60% to 70% of people with diabetes are affected by DPN, although a majority of these individuals are unaware of their nerve disease because they have no symptoms. DPN, if left undiagnosed and unmanaged, can result in the development of lower extremity ulcers and, in severe cases, amputation. It is estimated by the ADA that over 75% of all foot amputations are in patients with DPN. Other neuropathies may be present in as many as 30% of patients with diabetes, including CTS, radiculopathy and chronic inflammatory demyelinating polyneuropathy, or CIDP.

Low back pain. Low back pain can have many causes. When low back pain has a neurological source, it is often focal in nature and associated with pain that radiates from the lower back region into the leg, called sciatica. In some cases, the patient may also experience loss of

sensation and weakness in the lower leg. In advanced cases, these symptoms can become disabling. The symptoms result from pressure on the nerve roots, the precursors of the nerve, as they exit the spine. The source of the pressure is usually part of an intervertebral disc that is displaced from its normal location between the vertebral bodies. These disorders are often called herniated or ruptured discs.

CTS. CTS, is caused by swelling of the tendons that traverse the wrist alongside the median nerve. The swollen tendons compress the median nerve, resulting in damage to the nerve that leads to numbness in the first three fingers of the hand, weakness in the thumb, and occasionally wrist and hand pain. CTS is the most common focal neuropathy.

Other medical conditions associated with neuropathies. Common chronic disorders such as obesity, rheumatoid arthritis and spinal stenosis, or narrowing of the spinal canal, are commonly associated with neuropathies. In these complicated cases, it is particularly important for the physician to confirm or exclude neuropathies in order to develop effective treatment programs.

Nerve damage caused by chemotherapy. A number of widely used chemotherapeutic agents are toxic to nerves. Unfortunately, by the time patients report symptoms, significant nerve damage has often already occurred.

Limitations of Traditional Methods for Detecting Neuropathies

Neuropathies have traditionally been evaluated using clinical and diagnostic methods but there are limitations to these methods. The clinical examination is qualitative rather than quantitative, it is subjective and it does not often detect pre-clinical or early stage disease. Traditional nerve conduction studies and NCS/nEMG procedures are performed under a referral to a neurologist and this referral process can result in delays and inconvenience for the patient, higher expense and loss of control of the patient's care by the referring physician. Traditional procedures are complex and are therefore only performed by a small number of physicians, such as neurologists, and the testing is therefore not generally widely available. In addition, traditional procedures may be painful if an nEMG procedure is involved since the physician will insert needles into the patient's muscles often in close proximity to the site of pain.

NeuroMetrix Solution/NC-stat System

The NeuroMetrix point-of-service neurodiagnostic solution is known as the NC-stat System. The NC-stat System is comprised of: (1) disposable single use biosensors that are placed non-invasively on the patient's body, (2) the NC-stat device and related components and (3) the NC-stat docking station, an optional device that enables the physician to transmit data to our onCall Information System. The onCall Information System formulates the data it receives for each test into a detailed report that is sent to the physician via facsimile or e-mail in three to four minutes on average and provides raw data and information for the physician to consider along with the clinical examination of the patient and other information in diagnosing a patient's condition. The NC-stat System assists the physician in rapidly and accurately examining the patient in a manner that may be cost-effective for the patient and third-party payer.

Biosensors. The biosensors are single use, self-adhesive, nerve-specific, electrodes that are placed on the body and connected to the NC-stat device. Through the use of a specialized gel and a digital thermometer, both of which are contained within the biosensors, nerve signals are converted to electronic data that can be received and displayed by the NC-stat device. Currently, we sell biosensors for assessment of nerve function in the median and ulnar nerves in the upper extremities for the diagnosis of CTS and for assessment of the nerve function in peroneal, tibial and sural nerves in the lower extremities for the diagnosis of DPN and low back conditions.

The biosensors are designed to be positioned according to common anatomical landmarks with a configuration that facilitates correct placement. We designed the biosensors so that they could be applied with minimal training by members of a physician's clinical staff. In a typical nerve conduction study, multiple nerves are evaluated and multiple biosensors are used according to general guidelines established by the Center for Medicaid and Medicare Services, or CMS, and physician associations.

NC-stat device. The NC-stat device is designed for efficient use by the physician or a member of the physician's clinical staff. The NC-stat device can only be operated with our biosensors. This instrument customizes and calibrates the test for each patient, analyzes neurophysiological signals collected from the biosensor and displays the pertinent results on an liquid crystal display, or LCD screen immediately at the conclusion of each nerve conduction study. It also stores data from multiple patients for optional transmission to the onCall Information System. We also sell optional related components that allow for the testing of long nerve segments, such as those between the elbow and wrist or the knee and foot. The NC-stat device contains software that performs all the control and analysis algorithms necessary to carry out a nerve conduction study. A complete nerve conduction study may be performed with just the device and the biosensors. Another device for the assessment of potential neuropathic conditions, the ADVANCE System, is under 510(k) review by the FDA.

NC-stat docking station and onCall Information System. The NC-stat docking station is an optional device that automatically transmits data from the NC-stat device via telephone line, such as those used by facsimile machines, to the onCall Information System that we maintain. The data is automatically processed by the onCall Information System and stored in a central database, and a detailed computer generated report is created for each patient that is then sent to the physician via facsimile or e-mail in three to four minutes on average. The report includes the raw waveform data, comparisons to an age-adjusted and height-adjusted normal range population, study reference table and text summaries of the study, which provides additional information and a convenient summary of the study to assist the physician in the diagnosis of the patient. Although the study data presented in the onCall Information System report can be generated manually by the physician using the numerical measurements displayed by the NC-stat device, the report is a convenient and fast adjunct. Whether using the information from the onCall Information System report or the NC-stat device display, the actual clinical interpretation of the NC-stat System results is always performed by the physician ordering the study. The onCall Information System can also provide daily, monthly and quarterly reports to customers. These reports provide assistance in correct submission for third-party reimbursement and assist in tracking overall clinical utilization. The onCall Information System generally is available 24 hours per day, seven days per week. Although purchase of the NC-stat docking station and utilization of the onCall Information System are entirely optional, we believe substantially all of our customers use this system in all studies they conduct with the NC-stat System. We currently have a record of over three million individual nerve tests within the onCall Information System database. We believe that this information provides us with the ability to continually improve our products and provide our customers with a very high level of customer service and value. During the fourth quarter of 2006, at the request of the FDA, we submitted a 510(k) filing relating to portions of the onCall Information System currently in use. Depending on the outcome of the FDA's review, we may be required to modify or remove the aspects of the onCall Information System that are under review, which may make the NC-stat System more difficult to use by physicians. We are currently in the process of responding to the second additional information request that we have received from the FDA relating to this filing.

Recognizing the opportunity created by what we believe are the limitations of traditional diagnostic methods coupled with the availability of current and potential new treatments for certain neuropathies,

NeuroMetrix has developed the NC-stat System for the performance of non-invasive nerve conduction studies at the point-of-service. Our proprietary technology provides physicians with an in-office diagnostic system that assists physicians in performing rapid and accurate examinations that may be cost-effective for the patient and third-party payer. We believe that the NC-stat System represents a significant advance in neurological diagnostics and offers an improvement over traditional diagnostic procedures with the following benefits:

Facilitates performance of nerve conduction studies at the point-of-service. The complexity and high capital cost of traditional diagnostic methods generally have limited their use to neurologists and physicians in related specialties. We believe the features of the NC-stat System facilitate the performance of nerve conduction studies within the offices of a wide range of physicians, including primary care and specialist physicians. By allowing nerve conduction studies to be performed in the primary care or specialist physician's office, the patient can avoid the expense and inconvenience of a referral visit. Additionally, the NC-stat System enables primary care and specialist physicians to retain greater control over their patients by eliminating the need to refer them out for a traditional NCS/nEMG procedure.

Provides a cost-effective diagnostic tool. We believe that the NC-stat System could potentially reduce the cost to the patient and third-party payer of many nerve conduction studies. This belief is based on our observation that when these procedures are performed by the physician with primary clinical responsibility for the patient, the study is more directed so that generally fewer nerves are tested without compromising accuracy. As the cost to third-party payers for nerve conduction studies is typically based on the number of nerves tested, use of the NC-stat System can result in lower costs to patients and third-party payers. When an nEMG procedure is also performed, the cost can be even higher.

Requires minimal capital investment. We sell the NC-stat System, with equivalent technical specifications to the more expensive traditional instruments, for a list price of approximately $6,000, compared with $15,000 to $40,000 for the cost of traditional NCS/nEMG equipment. We believe the lower capital cost of the NC-stat System will aid in the expansion of nerve conduction studies beyond neurologist offices.

Simple to operate. The biosensors are designed for ease in placement, which allows a wide range of physician office personnel to administer the technical portion of the study under the supervision of a physician. The NC-stat device utilizes software algorithms that perform each step of a nerve conduction study in a reliable manner, with embedded automation technology that addresses and minimizes the technical training requirements for performing nerve conduction studies, while also ensuring that the end results are accurate and reliable. We believe that, in combination, these features allow accurate and reliable nerve conduction studies to be performed in 15 to 30 minutes on average.

Patient-friendly, non-invasive procedure. The NC-stat System allows for reduced patient discomfort during the nerve conduction study by minimizing the magnitude of the electrical stimulus to the nerve via a proprietary patient-specific calibration procedure. We believe that in most cases, the sophisticated signal processing and automation capabilities of the NC-stat System provide sufficient diagnostic information to eliminate the need for an NCS/nEMG procedure. This saves the patient the discomfort, stress and risk of this invasive procedure.

Neurovascular Disease

Diabetic retinopathy is a neurovascular disease and is one of the most serious complications of diabetes. Diabetic retinopathy is the leading cause of blindness in adults age 20 to 65. Microvascular complications caused by diabetes can lead to retinopathy and if untreated can result in vision loss and even blindness. Twenty years after diagnosis nearly all patients with Type I diabetes have some degree

of diabetic retinopathy and 60% of all patients with Type II diabetes have some degree of retinopathy, even though many may not have symptoms.

Over time, diabetes affects the circulatory system of the retina. The earliest phase of the disease is known as background diabetic retinopathy. In this phase, the arteries in the retina become weakened and leak, forming small, dot-like hemorrhages. These leaking vessels often lead to swelling or edema in the retina and decreased vision. The next stage is known as proliferative diabetic retinopathy. In this stage, circulation problems cause areas of the retina to become oxygen-deprived, or ischemic. New, fragile, vessels develop as the circulatory system attempts to maintain adequate oxygen levels within the retina. This is called neovascularization. Unfortunately, these delicate vessels hemorrhage easily. Blood may leak into the retina and vitreous, causing spots or floaters, along with decreased vision. In the later phases of the disease, continued abnormal vessel growth and scar tissue may cause serious problems such as retinal detachment and glaucoma. Ultimately, if untreated, diabetic retinopathy can lead to loss of vision or blindness.

The traditional approach to the detection of retinopathy in patients with diabetes is a referral to an eye specialist, such as an ophthalmologist, for an assessment. In spite of the recommendation by the ADA that all patients with diabetes have an annual dilated eye examination, only approximately 50% of these patients are actually complying and being tested on an annual basis. Treatments such as laser surgery are available for patients diagnosed with diabetic retinopathy and the earlier the condition is detected the more likely a favorable outcome.

The DigiScope

The DigiScope was developed by EyeTel in clinical partnership with the Wilmer Opthalmological Institute at Johns Hopkins University for the risk assessment of retinopathy. We acquired substantially all of the assets and assumed certain liabilities of EyeTel, including all rights to the DigiScope, on December 26, 2007.

The DigiScope has a fully integrated digital fundus camera which allows for the capture of high quality dilated retinal images in approximately ten minutes. The test is performed in primary care physicians' offices, optometry clinics and vision centers and the images obtained are sent electronically to the Wilmer EyeTel Reading Center and are read by retinal specialists. The results are reviewed by the physician or optometrist and a referral will be made to the eye specialist, such as an ophthalmologist, if clinically relevant abnormalities are detected. The test using the DigiScope can be easily administered by the physician's clinical staff under the supervision of the physician and requires minimal training. The DigiScope system is self-prompting, has a touch screen and audible cues for simple operation. The DigiScope examination is acceptable as an annual diabetic eye examination under the Health Plan Employer Data and Information Set, or HEDIS, 2004 technical specifications.

Market Opportunity

NC-stat System

The sensitivity of the nervous system to metabolic and mechanical damage, compounded by its limited regenerative ability, creates a market opportunity for a medical device that can assist in point-of-service diagnoses of neuropathies in a manner that is cost-effective for the patient and third-party payer. We believe that the availability of point-of-service nerve conduction studies will result in earlier detection of neuropathies, leading to earlier therapeutic intervention and, in many cases, improved clinical and economic outcomes. We believe that use of traditional NCS/nEMG procedures is limited by the referral process and the resulting delay in availability of diagnostic information, the inconvenience and discomfort of these methods for the patient, and the expense to the patient and third-party payer. Our policy is to promote and support the utilization of nerve conduction studies in a manner strictly consistent with prevailing guidelines on the medically appropriate use of this diagnostic

procedure. We estimate that there are approximately two million traditional NCS/nEMG procedures currently performed each year in the United States. The most common indication for which the NC-stat System has been used historically is CTS. CTS represented approximately 40% of total nerve conduction testing by our customers in 2007, while DPN and low back pain represented the balance of the testing performed. Based on our analysis of current patient data, we estimate that the potential for point-of-service nerve conduction studies in the diabetes, low back pain and CTS markets in the aggregate could be greater than 9.5 million annual patient tests, estimated to be more than $1.0 billion annually for our disposable biosensors, in the United States. However, market size is difficult to predict, and we cannot assure you that our estimates will prove to be correct. We believe that additional applications of a point-of-service product offering such as the NC-stat System, including the clinical assessment of patients with neuropathies caused by or associated with other clinical disorders, could further increase this potential market size. We believe a potential opportunity in the international markets exists for the NC-stat System. We recently launched the NC-stat System into the U.K. on a limited basis through a local distributor of medical device products.

DigiScope

The high level of incidence of diabetic retinopathy and its serious complications creates a market opportunity for a device that can be used by primary care physicians and endocrinologists as well as optometrists at the point-of-service for the early detection of diabetic retinopathy. There are estimated to be 21.0 million people in the United States with diabetes and this total is expected to grow. Diabetic retinopathy is the leading cause of blindness in adults age 20 to 65. Twenty years after diagnosis nearly all patients with Type I diabetes have some degree of diabetic retinopathy and 60% of all patients with Type II diabetes have some degree of retinopathy, even though many may not have symptoms. The ADA recommends an annual dilated eye examination for all patients with diabetes. In spite of this recommendation, only approximately 50% of patients with diabetes actually receive an annual eye examination. This has created an opportunity for such testing to be performed in the primary care physician or endocrinologist office and optometry clinics and vision centers since these patients with diabetes are routinely seen by these care providers.

Market Size

We estimate that there are approximately 2.0 million traditional NCS/nEMG procedures currently performed each year in the United States. This estimate is based on (1) data from a Centers for Disease Control and Prevention, or CDC, report in 1996 regarding NCS/nEMG procedures ordered or performed during ambulatory patient visits and (2) data from a 2001 CMS report regarding Medicare reimbursement. We anticipate that the advantages and increased availability of point-of-service products such as the NC-stat System could potentially increase the number of nerve conduction studies performed.

We estimate the potential DPN market for a point-of-service product offering such as the NC-stat System could be over six million annual patient tests. The number of individuals with diabetes in the United States was estimated to be 21.0 million, or 7.0% of the population. Among this group, approximately 6.0 million were undiagnosed. According to the CDC, there are about 26.0 million annual patient visits to office-based physicians for diabetes. We anticipate that the increasing focus on early detection and prevention of the chronic complications of diabetes will lead to increased nerve conduction studies for DPN. We believe that the estimated 50% rate of annual foot examinations in patients known to have diabetes is a reasonable estimate for the addressable testing market in diabetes. If these examinations were replaced by a nerve conduction study, or a nerve conduction study were added to the examination, the diabetes arena would represent an opportunity for over six million annual NC-stat System patient tests. The number of Americans with diabetes is projected to more than double over the next 40 to

50 years. At the present time, there are no currently marketed pharmaceuticals targeted specifically at DPN, and therefore nerve conduction studies are performed on a selective basis in order to address specific clinical issues and to provide differential diagnosis. If a targeted therapy for DPN were successfully developed and marketed, we believe the rate of testing would further increase. Based on current clinical trial activity, we do not believe there are any therapies for DPN that appear to have an opportunity for commercial launch within the next two years.

We estimate the potential low back pain market for a point-of-service product offering such as the NC-stat System could be as great as three million annual patient tests. Low back pain is one of the most common medical conditions in the United States. Back disorders account for over one-quarter of all nonfatal occupational injuries and illnesses that result in days away from work. According to the CDC, there are about nine million annual patient visits to office-based physicians specifically for low back symptoms. The CDC further estimates that about one-third of office visits are initial visits, at which time we believe utilization of the NC-stat System is most likely. We thus anticipate that there may be as many as approximately three million testing opportunities for nerve conduction testing related to low back pain for a point-of-service product offering such as the NC-stat System. We believe that the number of testing opportunities may be even higher, as there are many patients that visit physicians for symptoms and medical conditions that must be differentiated from sciatica, such as leg and foot symptoms, rheumatoid arthritis and diabetes.

We estimate the potential CTS market for a point-of-service product offering such as the NC-stat System could be as great as 650,000 annual patient tests. CTS is a significant occupational issue, as the disorder results in the most days away from work among all major disabling workplace injuries and illnesses. In a health care survey published in the Journal of the American Medical Association, approximately 14% of adults reported symptoms characteristic of CTS. It was further estimated that 2.5% of adults have true CTS, which could be confirmed by clinical examination and nerve conduction studies. This is equivalent to approximately five million individuals in the United States. Over 350,000 surgeries are performed annually for CTS. The surgical procedure is called a carpal tunnel release, or CTR. Most third-party payers require a nerve conduction study prior to authorizing CTR surgery. According to the CDC, there are more than two million annual visits to office-based physicians for which CTS is the primary diagnosis. The CDC estimates that about one third of CTS-related office visits are initial visits, at which time we believe utilization of a point-of-service nerve conduction product offering is most likely. As a result, we estimate that there may be as many as 650,000 testing opportunities for a point-of-service product offering such as the NC-stat System related to CTS. We further believe that this estimate is conservative, as there are many patients that visit physicians for hand and wrist pain, or medical conditions with a high association with CTS such as rheumatoid arthritis, diabetes and obesity. We also anticipate that the high costs of CTS-related workers' compensation claims could motivate employers to increasingly use a point-of-service product offering such as the NC-stat System to pre-screen and monitor employees for CTS.

Based on the data outlined above, we estimate that the potential market size for a point-of-service product offering such as the NC-stat System for nerve conduction studies in the diabetes, low back pain and CTS markets in the aggregate could be greater than 9.5 million annual patient tests in the United States. We estimate that the potential market for a point-of-service product offering such as the NC-stat System could be more than $1.0 billion annually in the United States.

We estimate that the size of the market for a point-of-service product such as the DigiScope for the detection of diabetic retinopathy could be nearly $700 million. There are estimated to be 21.0 million people in the United States with diabetes and it is estimated that 15.0 million have actually been diagnosed with diabetes. The American Diabetes Association recommends an annual eye

examination for all people with diabetes. Using an annual eye examination fee of $45 per patient, this represents a potential market size of nearly $700 million.

Market size is difficult to predict, and we cannot assure you that our estimates will prove to be correct. We believe that additional applications of a point-of-service product offerings such as the NC-stat System and the DigiScope could further increase this market size. Additionally, although we have not yet quantified the size of the market, we believe a potential international market opportunity exists for the NC-stat System and for the DigiScope. The potential market opportunity is dependent on a number of factors including favorable reimbursement by third-party payers. There are no assurances that third-party payers will reimburse for an increasing level of nerve conduction studies at present levels or at all. Additionally, as there have been a number of adverse developments relating to the reimbursement for nerve conduction studies performed with the NC-stat System, our ability to access this market opportunity may be limited.

Clinical Studies and Clinical Validation

The performance of the NC-stat System has been substantiated in clinical studies that we have supported, the results of which have been published in peer-reviewed medical journals or presented at major medical conferences.

In studies published in the April 2000 issue of the *Journal of Occupational & Environmental Medicine*, the September 2000 issue of *Neurology and Clinical Neurophysiology* and the May 2004 issue of the *Journal of Hand Surgery*, the correlation between the results generated by the NC-stat System and traditional nerve conduction studies in measuring nerve function of 198 patients was examined. The correlation was equivalent to that found between different neurologists performing traditional nerve conduction studies.

A study published in the December 2002 issue of *Spine* evaluated the ability of the NC-stat System to detect neurological impairment in 25 patients with sciatica, confirmed by MRI and clinical examination. The diagnostic accuracy of the NC-stat System was equivalent to traditional NCS/nEMG procedures as documented in several other published studies.

In a study published in the August 2005 *American Journal of Orthopedics*, the clinical utility of the NC-stat System was assessed in 72 patients with CTS. The NC-stat System was found to have a high correlation with traditional laboratory testing. The NC-stat System also measured statistically significant improvement in median nerve function six months following CTR surgery.

In a study published in the August 2006 *Diabetes Care*, the NC-stat System was shown to be comparable to conventional nerve conduction testing in a group of 72 patients with diabetes tested for DPN.

In a study published in the December 2006 *Diabetes Technology and Therapeutics*, the use of the NC-stat System in 1,400 patients with diabetes in 28 primary care/endocrinology clinics was assessed in a prospective open-label study. The NC-stat System identified nerve conduction abnormalities in 75% of patients, and over 50% had results suggestive of diabetic polyneuropathy. The NC-stat System identified meaningful levels of neuropathy in patients within ADA recommended blood glucose control and in those newly diagnosed with diabetes.

In a study published in the January 2007 *Physiological Measurements*, the validity of NC-stat System lower extremity nerve measurements was assessed in 60 patients referred to a Veterans Administration electrodiagnostic laboratory. The authors concluded "This study shows that the technology used by the NC-stat System for studying the peroneal and posterior tibial nerves compares favorably.... with that obtained with traditional EMG equipment used under neurologist supervision."

In the January-February 2007 *Journal of the American Board of Family Medicine*, a retrospective blinded study of NC-stat System utilization by 613 family medicine, primary care, and internal medicine physician practices was conducted. Over a two-week period 1,190 patients underwent NCS for evaluation of CTS. A total of 31% of tested limbs yielded normal results, 53% indicated CTS, and the remaining studies identified other neuropathies. The authors concluded "This study demonstrated that point-of-service NCS by physicians for CTS was applied to appropriate patient subpopulations, was performed in accordance with evidence-based testing parameters, and generated relevant diagnostic outcomes."

An article published in the Winter 2007 issue of *Perspectives on Biological Medicine*, contrasted our nerve conduction study technology with traditional NCS/nEMG procedures, examined the ways in which computer-based electrodiagnostic equipment serves as a disruptive innovation, addressed challenges that need to be overcome to support widespread adoption of the new technology, and discussed the opposition generated by its use among stakeholders in traditional NCS/nEMG.

A study published in the November/December 2007 issue of *Electromyography and Clinical Neurophysiology* examined 34 patients with clinical findings consistent with a lumbosacral radiculopathy, or LSR, who had both nerve conduction study with NCS/nEMG and a NC-stat System based multi-parameter electrodiagnostic study. The study concluded that "EDX [electrodiagnostic] information other than NCS/nEMG can be important in the evaluation of patients with possible LSR."

In a study published in the March 2008 issue of *Diabetes Care*, 72 consecutive patients with diabetes underwent a full neurological examination and a concurrent evaluation for nine standard electrophysiological parameters using conventional nerve conduction studies (the reference standard) and a point-of-care device (NC-stat System). Based on the study results, the authors concluded that "A novel point-of-care device [NC-stat System] has reasonable diagnostic accuracy and thus may represent a sufficiently accurate alternative for detecting the diffuse electrophysiological criteria necessary to make the diagnosis of diabetic sensorimotor polyneuropathy."

A study published in the March 2008 issue of *Journal of Diabetes Science and Technology* analyzed 63,779 nerve conduction studies performed by more than 3,400 physician practices using the NC-stat System. For over 70% of the patients, the specific diagnostic question of the presence of diabetic polyneuropathy was addressed by nerve conduction studies with evidence-based criteria. The rate of diabetic polyneuropathy was found to be comparable to levels seen by academic electromyography laboratories. This study demonstrated that nerve conduction studies using computer-based electrodiagnostic equipment was a suitable tool for the diagnosis of diabetic polyneuropathy in large populations.

We continue to support well-designed clinical research studies utilizing the NC-stat System that are designed to demonstrate its clinical accuracy and cost-effectiveness. In addition, several clinical studies and trials have been performed, and others are underway, in which the NC-stat System is used to measure changes in nerve function. The NC-stat System was utilized by Eli Lilly in a clinical trial of Cymbalta for the treatment of pain associated with DPN.

The performance of the DigiScope has been validated in clinical studies, the results of which have been published in peer-reviewed medical journals as highlighted below.

In a study published in the May 2002 issue of *Investigational Ophthalmology and Visual Science*, the conclusions drawn were that "the DigiScope fulfills the instrumental requirements for a practical and cost-effective tool to acquire data needed to identify diabetic patients who must be referred to an eye care specialist." The study further concluded that the "DigiScope may help reduce the risk of vision loss in.....individuals who currently do not undergo an annual eye examination."

In a study of over 2,700 patients published in a 2006 issue of *Telemedicine and e-Health,* the conclusions were that the "DigiScope can be used in the primary care setting to identify patients with diabetes not currently under the care of an eye specialist who require referral to an ophthalmologist for evaluation and management of retinopathy."

Customers

We market our products directly to primary care and specialist physicians and clinics. We plan to begin marketing the DigiScope to optometrists in 2008. The NC-stat System provides primary care physicians and other physicians including orthopedic surgeons, endocrinologists, rheumatologists, and pain medicine physicians, who previously were not performing a nerve conduction study at the point-of-service or were referring these patients to a neurologist for a traditional NCS/nEMG procedure, with a product that can potentially improve the care of their patients and with a potential new source of revenues. As of December 31, 2007, we had over 5,500 active NC-stat customers. No single customer accounted for more than 10% of our revenues in 2007, 2006 or 2005.

Currently, there are approximately 190 customers using the DigiScope. We launched our sales and marketing efforts for this product in the first quarter of 2007.

Strategic Alliance

In November 2007, we entered into a strategic alliance with Cyberkinetics, a medical device company focused on neurological conditions. We made an investment of $2.5 million in shares of Cyberkinetics common stock and agreed to negotiate the terms of a joint venture with Cyberkinetics. In February 2008, we formed PNIR (Peripheral Nerve Injury Repair) LLC, a joint venture with initial ownership of 50% by NeuroMetrix and 50% by Cyberkinetics, and entered into a Collaboration Agreement and Operating Agreement with them. The focus of the joint venture is on the development and commercialization of a product for the treatment of peripheral nerve injury using the Andara OFS (Oscillating Frequency Stimulation) technology licensed by Cyberkinetics from Purdue University and using other technologies to be developed. The Andara OFS technology utilizes an oscillating electrical field to stimulate the regeneration of injured nerves and has been shown in initial human clinical studies to provide a statistically significant improvement in sensory and motor function of patients with acute spinal cord injuries.

Together with Cyberkinetics, we are in the preclinical stage of development of this product, which we expect will require the filing of a premarket approval application, or PMA, with the FDA. Under the terms of our joint venture agreement with Cyberkinetics, we have agreed to fund the first $2.0 million of program costs under the joint venture and any required funding beyond the initial $2.0 million will be shared equally by NeuroMetrix and Cyberkinetics. Cyberkinetics has agreed to contribute the Andara OFS technology and certain additional technology, know-how and intellectual property. Cyberkinetics will manufacture products commercialized under the agreement and we have received sales and marketing rights to all products commercialized under the joint venture. The two companies have agreed to charge the joint venture at actual cost for all expenses associated with the manufacturing of the products commercialized under the agreement and all expenses associated with the sales and marketing of the products commercialized.

There are estimated to be approximately 800,000 peripheral nerve injuries annually and it is believed that at least 100,000 of these injuries could benefit from electrical stimulation to provide neural repair and regeneration. It is believed that the market opportunity for a therapeutic for peripheral nerve injury is substantial.

As part of the strategic alliance, NeuroMetrix also received a right of first negotiation for the commercialization and distribution rights in North America to a product under development by Cyberkinetics for the treatment of acute spinal cord injury using the Andara OFS technology. This right

expires on December 31, 2008. Cyberkinetics has filed a Humanitarian Device Exemption, or HDE, with the FDA for this product, since there are fewer than 4,000 patients who could potentially benefit from the Andara OFS product. The product consists of a device which is implanted in close proximity to the spine and a series of electrodes which are attached to the spine above and below the site of the spinal cord injury. The implant remains in place for approximately 15 weeks and is then removed. The market opportunity for the Andara OFS device for acute spinal cord injury is believed to be as large as $150 million annually. There are no assurances that Cyberkinetics will receive FDA approval of their HDE filing and there are no assurances that we will be able to successfully obtain the commercialization and distribution rights to the product.

We also obtained a first right of negotiation to acquire Cyberkinetics and this right expires on December 31, 2008.

Geographic Information

Substantially all of our assets, revenues and expenses for the years ended December 31, 2007, 2006 and 2005 were located at or derived from operations in the United States. As a result of the launch of the NC-stat System in the United Kingdom, which has been on a limited basis to date, we had initial revenues from sales outside the United States beginning in the third quarter of 2007.

Sales, Marketing and Distribution

Currently, we employ 50 regional sales managers, 5 regional sales directors and a national sales director who sell directly to physician practices. During 2007, we terminated the relationships we had with independent sales agencies including national firms such as Physician Sales & Service and Henry Schein, Inc. Our products are primarily marketed and distributed within the United States, although we initiated sales efforts in the United Kingdom during the third quarter of 2007.

We launched our sales and marketing efforts for the DigiScope product for the detection of diabetic retinopathy in the first quarter of 2007. This product is being sold directly to primary diabetes care physicians through our sales force. The DigiScope is being marketed to our installed base of NC-stat System customers and to potentially new physician office customers. We obtained an exclusive sales and marketing license to the DigiScope from EyeTel in the fourth quarter of 2006 for the primary diabetes care market and acquired substantially all of the assets and assumed certain liabilities of EyeTel on December 26, 2007, expanding the market opportunity into the optometry clinic and vision center market. We recently launched our sales and marketing efforts for the DigiScope into the optometry market. EyeTel had conducted pilot studies in a number of vision centers at Wal-Mart stores, For Eyes clinics and CostCo clinics. Our sales force plans to market the DigiScope to these vision centers starting in 2008 once a comprehensive sales and marketing strategy has been developed.

We invest significant efforts in technical, clinical and business practices training for our regional sales managers. We also require each sales representative to attend periodic sales and product training programs. The efforts of our regional sales managers are enhanced by proprietary software tools that are accessed via a secure website, which we refer to as the sales portal. This portal gives our sales personnel access to real time customer sales and product usage information, various applications to help identify and close new business and marketing materials. The portal also provides customer relationship management functions.

We generally market our products directly to primary care and specialist physicians. The NC-stat System provides primary care and specialist physicians, who previously were not performing a nerve conduction study at the point-of-service or were referring these patients to a neurologist for a traditional NCS/nEMG procedure, with a product that can potentially improve the care of their patients and with a potential new source of revenues. We believe that there are important marketing advantages of the NC-stat System. The NC-stat System can potentially help to accelerate the diagnosis

of neuropathies by allowing primary care and specialist physicians to perform a nerve conduction study at the point-of-service rather than having to make a referral to a neurologist. We also market our products at various industry conferences in order to accelerate the market awareness of our products, and market adoption for our products.

We are evaluating our options for sales and marketing of our products outside the United States. We will likely use distributors in these foreign markets given their direct understanding of each relevant market and the unique requirements of selling products in each market. Consistent with this strategy, we recently launched our sales efforts for the NC-stat System on a limited basis into the United Kingdom through a distributor of medical device products, representing our initial commercial sales in Europe. We expect to sell our products such as the NC-stat System in Europe through distributors who will stock inventory and ship product and bill directly to customers.

We generally invoice products purchased by our customers directly to physician offices and other customers. Our regional managers are compensated by a combination of base salary, commissions and goal-based bonus compensation.

Our success is highly dependent on our ability to maintain our direct sales force. In markets outside the United States, we may be unable to enter into agreements with qualified distributors on commercially reasonable terms or at all and we may not be successful in maintaining the existing sales and marketing infrastructure we have developed. Even if we are able to enter into agreements with distributors outside the United States, these parties may not commit the necessary resources to effectively market and sell our products or ultimately be successful in selling our products.

Promotion and sales of medical devices are also highly regulated not only by the FDA, but also by the Federal Trade Commission, and, outside the United States, by other international bodies, and are subject to federal and state fraud and abuse enforcement activities.

We have products in development that, if successfully commercialized, may require us to develop a separate specialized sales force to call on anesthesiologists or other specialists.

Manufacturing and Supply

We rely on outside contractors for the manufacture and servicing of our products and their components, and we do not currently maintain alternative manufacturing sources for the NC-stat monitor, docking station or biosensors, the DigiScope or any other finished goods products. In outsourcing, we target companies that meet FDA, International Organization for Standardization, or ISO, and other quality standards supported by internal policies and procedures. Supplier performance is maintained and managed through a corrective action program ensuring all product requirements are met or exceeded. We believe these manufacturing relationships minimize our capital investment, provide us with manufacturing expertise and help control costs.

Following the receipt of products or product components from our third-party manufacturers, we conduct the necessary inspection and packaging and labeling at our corporate headquarters facility. We may consider manufacturing certain products or product components internally, if and when demand or quality requirements make it appropriate to do so. We currently have no plans to manufacture any products or product components internally.

We seek to obtain products from our manufacturers in order to maintain sufficient inventory to satisfy our customer obligations. We did not experience any inventory shortages on any established products in 2007, although we did experience some delays in production with Parlex Corporation, or Parlex, the manufacturer of our biosensors. If our third-party manufacturers are unable to manufacture our products to keep up with demand, we would not meet expectations for our business.

Parlex has been manufacturing our NC-stat biosensors since early 1999. In August 2006, we entered into a mutually exclusive manufacturing and supply agreement with Parlex pursuant to which Parlex will manufacture and supply to us, and we will purchase from Parlex, at agreed upon prices per unit, all of our requirements of biosensors for resale in the United States. Under the agreement, Parlex has agreed not to manufacture biosensors to be used to measure nerve conduction for any other company during the term of the agreement and, in some cases, for a period of one year thereafter. Either party may terminate the agreement at any time upon not less than 18 months prior written notice, provided that neither party may terminate the agreement prior to August 2, 2008. Parlex manufactures our biosensors at a facility in Massachusetts and also has the ability to perform certain manufacturing steps for our biosensors at a second site located in the United Kingdom. We have been working closely with Parlex on certain production issues they have experienced which we believe relate primarily to the transition of manufacturing of our biosensors to a new facility operated by Parlex. We have experienced an increase in the number of biosensors that have not produced a usable result when used by our customers and have been working to resolve this issue with Parlex.

Sunburst EMS, Inc., or Sunburst, has been manufacturing our NC-stat monitors and docking stations since November 2005. We signed a formal supply agreement with Sunburst during 2006 for the continued manufacturing and supply of our diagnostic devices. Sunburst manufactures the current generation of the NC-stat diagnostic devices and the ADVANCE System at a facility in Massachusetts.

The DigiScope is manufactured by TopZone Electronics, Inc., or TopZone, a manufacturer located in China. We currently purchase DigiScopes from TopZone through purchase orders rather than a formal manufacturing agreement.

We and our third-party manufacturers are registered with the FDA and subject to compliance with FDA quality system regulations. We are also ISO registered and undergo frequent quality system audits by European agencies. The NC-stat System and the DigiScope are cleared for marketing within the United States and Canada, and the NC-stat System is also approved for marketing in the European Union, although to date our sales have been primarily in the United States. Our facility and the facilities of our manufacturers are subject to periodic inspections by regulatory authorities, and may undergo compliance inspections conducted by the FDA and corresponding state agencies. We were inspected by the FDA in May 2003. During its inspection, the FDA issued a Form 483, which is a notice of inspection observations. Two minor items were identified and the corrective actions for both were initiated prior to the completion of the audit. The responses provided to the FDA were deemed adequate and no further action has been requested. As a registered device manufacturer, we and our manufacturers will undergo regularly scheduled FDA quality system inspections. However, additional FDA inspections may occur if deemed necessary by the FDA.

Products Under Development and Research and Development

Our research and development efforts are focused in the near term on further enhancing our existing products, which includes developing the ADVANCE System and new nerve conduction electrodes, as well as developing the NAVIGATOR platform, a system for the minimally invasive delivery of drugs and other therapeutic agents for regional anesthesia, pain control and local treatment of neuropathies by both specialist physicians and primary care physicians.

Our research and development staff consists of 33 people, including seven who hold Ph.D. or M.D. degrees. Our research and development group has extensive experience in neurophysiology, biomedical instrumentation, signal processing, biomedical sensors, optics and information systems. These individuals work closely with our marketing group, our clinical support group (led by a board-certified neurologist), our scientific advisors and our customers to design products that are intended to improve clinical outcomes.

Devices for Regional Anesthesia, Pain Control and the Treatment of Neuropathies

In pursuit of our objective to develop medical devices that provide solutions for the diagnosis and treatment of patients with nervous system disorders, including neuropathies, and neurovascular diseases and that provide solutions for regional anesthesia and pain control, we are expanding our product base beyond the diagnostic arena and into the treatment arena. We believe that our core technology can be adapted and extended to provide minimally invasive approaches to nerve localization and specifically to provide regional anesthesia, pain control and treatments for neuropathies. We are developing the NAVIGATOR platform, a proprietary neuro-electrical guidance system, that is designed to help physician's position drug delivery devices such as hypodermic needles and catheters safely and quickly in very close proximity to specific nerves to optimize the therapeutic benefit.

The use of nerve localization instrumentation and needles is a standard of care for nerve block procedures which are increasingly the preferred form of anesthesia for many surgical procedures, particularly within orthopedics. This can effectively provide the physician with confirmation that the needle is in the proper location and can optimize the efficacy of anesthetic delivery.

We believe that neuropathies, that are focal in nature, can be safely and effectively treated if drugs can be delivered near the disease site without damaging the nerve in the process. Some of these types of treatments are performed today, but they are performed manually by a limited number of physicians. Our NAVIGATOR development program includes the design of a product version that we believe will reduce the risk involved in providing these treatments.

Current approaches to regional anesthesia and nerve block include ultrasound and some alternative approaches to nerve localization. Clinical studies have been performed by third parties that demonstrate that the two approaches, ultrasound and nerve stimulation, are comparable. The limitations of ultrasound include the fact that a high level of expertise and training is required, there is no objective evidence that a nerve has been successfully blocked, and there may be difficulty in visualizing the tip of the injection needle. While the current generation of nerve localization technology is generally effective, it is limited with respect to both accuracy and usability and confirmation of the effectiveness of the treatment is subjective. Based on discussions with anesthesiologists, we believe that there is a need for improvements in nerve localization products that may be provided by our NAVIGATOR platform.

After establishing our technology in anesthesia, we plan to proceed into the broader market for select clinical conditions such as the treatment and management of CTS and common pain syndromes.

We expect that our NAVIGATOR products will resemble our diagnostic products in that there will be three key components:

consumables that will include proprietary nerve localization and drug delivery needles;

electrodes and other disposables; and

an electronic instrument linked to our onCall Information System.

There are no assurances that our devices for regional anesthesia, pain control and the treatment of neuropathies will be successfully developed, receive 510(k) clearance from the FDA and that, if launched, sales and marketing efforts will be successful.

NCS/nEMG Systems

We have an ongoing program of making enhancements and improvements to our nerve conduction products. We are developing new biosensors and associated software for the medically appropriate testing of additional nerves. We have also developed a more advanced diagnostic device, the ADVANCE System, for which we submitted a 510(k) filing to the FDA in 2007.

The ADVANCE System has a number of important innovations and features:

- Key technical and engineering specifications that we believe meet or exceed those of other electrodiagnostic devices on the market.
- Advanced signal processing algorithms that provide physicians with high quality and detailed nerve conduction data to incorporate into their diagnostic assessment. We have filed two patents on these algorithms.
- A user interface consisting of a high resolution color touch screen that allows physicians and their clinical staff to conduct accurate nerve conduction studies and other electrodiagnostic tests in a straightforward manner. This user interface provides for real-time data review including waveforms.
- Compatibility with existing disposables and with new electrode sets that we develop in the future.
- The capability to support the performance of nEMG studies.

Neural Repair and Regeneration

In February 2008, we formed PNIR (Peripheral Nerve Injury Repair) LLC, a joint venture with Cyberkinetics. The focus of the joint venture is on the development and commercialization of a product for the treatment of peripheral nerve injury using the Andara OFS technology licensed by Cyberkinetics from Purdue University and using other technologies to be developed within the joint venture. The Andara OFS technology utilizes electrical stimulation for the regeneration of injured nerves. Together with Cyberkinetics, we are in the preclinical stage of development of this product, which we expect will require the filing of a PMA with the FDA.

There are estimated to be approximately 800,000 peripheral nerve injuries annually and it is believed that at least 100,000 of these injuries could benefit from electrical stimulation to provide neural repair and regeneration. It is believed that the market opportunity for a therapeutic for peripheral nerve injury could be substantial.

As part of the strategic alliance with Cyberkinetics, we also received a right of first negotiation for the commercialization and distribution rights in North America to a product under development by Cyberkinetics for the treatment of acute spinal cord injury using the Andara OFS technology. This right expires on December 31, 2008. Cyberkinetics has filed an HDE with the FDA for this product, since there are fewer than 4,000 patients who could potentially benefit from the Andara OFS product. The product consists of a device which is implanted in close proximity to the spine and a series of electrodes which are attached to the spine above and below the site of the spinal cord injury. The implant remains in place for approximately 15 weeks and is then removed. The market opportunity for the Andara OFS device for acute spinal cord injury is believed to be approximately $150 million annually. There are no assurances that Cyberkinetics will receive FDA approval of their HDE filing and there are no assurances that we will be able to successfully obtain the sales and marketing rights to the product.

NEUROMetrix®, NC-stat®, ADVANCE , DigiScope® and onCall® are trademarks of ours. Andara and OFS are registered trademarks of Cyberkinetics.

During 2007, 2006 and 2005, we spent $4.9 million, $5.0 million and $3.8 million, respectively, on research and development.

Competition

We consider the primary competition for the NC-stat System to be traditional NCS/nEMG procedures. Our success depends in large part on convincing physicians to adopt the NC-stat System in order to perform nerve conduction studies at the point-of-service.

There are a number of companies that sell traditional NCS/nEMG equipment, typically to neurologists. These companies include Cardinal Healthcare (acquired Viasys Healthcare Inc. in 2007), Cadwell Laboratories, Inc and Natus (acquired Xltec, Inc. in 2007). Cardinal Healthcare has substantially greater financial resources than we do, and they have established a reputation as an effective worldwide distribution channel for medical instruments to neurologists and other physicians. Xltec, Inc. launched a product for the point-of-service nerve conduction studies market in 2006 and subsequently announced that they were withdrawing this product from the market. We are aware of one additional company, Neumed Inc., that markets a nerve conduction study system to the point-of-service market.

We believe that among systems marketed for the performance of nerve conduction studies today, only the NC-stat System provides the level of diagnostic accuracy, the level of automation and the ease of use required for successful penetration of the point-of-service market. We also believe that the reporting and data repository functions provided by the onCall Information System, although entirely optional, provide our customers who use this service with added value that is not matched by other currently marketed products. We further believe that the expanding database of nerve conduction study data captured by the onCall Information System facilitates our ability to improve the performance of the NC-stat System. We believe that the size of our database and ongoing improvements provide us with a significant competitive advantage.

There are a number of companies that sell equipment for the detection of eye disorders such as diabetic retinopathy. These companies, such as Optos plc, sell primarily to the ophthalmologist market rather than to the primary care, endocrinology and optometry markets.

Intellectual Property

We rely on a combination of patents, trademarks, copyrights, trade secrets and other intellectual property laws, nondisclosure agreements and other measures to protect our proprietary technology, intellectual property rights and know-how. We hold issued utility patents covering a number of important aspects of our NC-stat System. We believe that in order to have a competitive advantage, we must develop and maintain the proprietary aspects of our technologies. We also hold an exclusive license with Johns Hopkins University to manufacture, use and sell the DigiScope pursuant to a patent held by the university that will remain in-force until 2018. Currently, we require our employees, consultants and advisors to execute confidentiality agreements in connection with their employment, consulting or advisory relationships with us, where appropriate. We also require our employees, consultants and advisors, who we expect to work on our products, to agree to disclose and assign to us all inventions conceived during the work day, developed using our property or which relate to our business. Despite any measures taken to protect our intellectual property, unauthorized parties may attempt to copy aspects of our products or to obtain and use information that we regard as proprietary.

Patents

As of December 31, 2007, we had 16 issued U.S. patents, 21 issued foreign patents and 38 pending patent applications, including 25 U.S. applications, 4 International PCT applications and 9 foreign national applications. We also hold an exclusive license from the Massaschusetts Instiitute of Technology to two issued U.S. patents and two issued foreign patents. We hold an exclusive license to one U.S. patent and 5 foreign patents held by Johns Hopkins University to manufacture, use and sell

the DigiScope. The license also covers one additional pending foreign patent application. The issued and pending patents that we own and license cover, among other things:

Nerve conduction biosensors and related methods;

Nerve conduction hardware;

Algorithms for performing and analyzing nerve conduction studies;

NC-stat System industrial design; and

Opthalmic imaging service with certain capabilities.

Our issued design patents begin to expire in 2015, and our issued utility patents begin to expire in 2017. In particular, seven of our issued U.S. utility patents covering important aspects of our current products will expire on the same date in 2017. Although the patent protection for material aspects of our products covered by the claims of the patents will be lost at that time, we have additional patents and patent applications directed to other novel inventions that will have patent terms extending beyond 2017.

The medical device industry is characterized by the existence of a large number of patents and frequent litigation based on allegations of patent infringement. Patent litigation can involve complex factual and legal questions, and its outcome is uncertain. Any claim relating to infringement of patents that is successfully asserted against us may require us to pay substantial damages. Even if we were to prevail, any litigation could be costly and time-consuming and would divert the attention of our management and key personnel from our business operations. Our success will also depend in part on our not infringing patents issued to others, including our competitors and potential competitors. If our products are found to infringe the patents of others, our development, manufacture and sale of these potential products could be severely restricted or prohibited. In addition, our competitors may independently develop similar technologies. Because of the importance of our patent portfolio to our business, we may lose market share to our competitors if we fail to protect our intellectual property rights.

As the number of entrants into our market increases, the possibility of a patent infringement claim against us grows. Although we have not received notice of any claims, and are not aware that our products infringe other parties' patents and proprietary rights, our products and methods may be covered by U.S. patents held by our competitors. In addition, our competitors may assert that future products we may market infringe their patents.

A patent infringement suit brought against us may force us or any strategic partners or licensees to stop or delay developing, manufacturing or selling potential products that are claimed to infringe a third-party's intellectual property, unless that party grants us rights to use its intellectual property. In such cases, we may be required to obtain licenses to patents or proprietary rights of others in order to continue to commercialize our products. However, we may not be able to obtain any licenses required under any patents or proprietary rights of third parties on acceptable terms, or at all. Even if we were able to obtain rights to the third-party's intellectual property, these rights may be non-exclusive, thereby giving our competitors access to the same intellectual property. Ultimately, we may be unable to commercialize some of our potential products or may have to cease some of our business operations as a result of patent infringement claims, which could severely harm our business.

Trademarks

We hold domestic registrations for the marks NEUROMETRIX, NC-STAT, onCall and DIGISCOPE. We also hold certain foreign trademark registration's for the marks NEUROMETRIX and NC-STAT. Andara OFS (Oscillating Field Stimulator) is a registered trademark of Cyberkinetics.

Third-Party Reimbursement

Reimbursement from third-party payers is an important element of success for medical products companies. We anticipate that sales volumes and prices of our products will continue to be dependent in large part on the availability of reimbursement for our customers from third-party payers and on policies issued by governmental agencies. Third-party payers include governmental programs such as Medicare and Medicaid, private insurance plans, and workers' compensation plans. These organizations may deny coverage and refuse reimbursement for a diagnostic procedure or specific product such as our neuropathy diagnostic system, the NC-stat System, if they determine that the diagnostic test or product was not medically appropriate, reasonable or necessary. Tests will be considered not medically reasonable or necessary if they are deemed "investigational" (i.e. there is insufficient evidence of efficacy or accuracy.) The third-party payers may also attempt to place limitations on the types of physicians that can perform specific types of diagnostic procedures. Also, third-party payers are increasingly challenging the prices charged for medical products and services. In international markets, reimbursement and healthcare payment systems vary significantly by country, and many countries have instituted payment ceilings on specific product lines and procedures. We cannot assure you that procedures using our products will be considered medically reasonable and necessary for a specific indication, that our products will be considered cost-effective by third-party payers, that procedures performed using our products will be reimbursed as separate procedures under existing reimbursement codes, that an adequate level of reimbursement will be available or that the third-party payers' coverage and reimbursement policies will not adversely affect our ability to sell our products profitably.

As our presence in the market has expanded, we have experienced and are likely to continue to experience an increased focus from third-party payers and governmental agencies regarding the reimbursement of nerve conduction studies performed using the NC-stat System and an increased focus from these organizations regarding the professional requirements for performing nerve conduction studies in general. A number of third-party payers, including commercial payers, have taken and may continue to take the position of not reimbursing our customers for their use of the NC-stat System.

There are sixteen organizations serving as local insurance carriers that, on behalf of Medicare, process claims submitted by physician practice groups and other healthcare providers and establish what are called local coverage determinations, or LCDs. In the absence of a position issued by Medicare at the national level, the LCDs issued by these local insurance carriers govern the reimbursement of procedures performed using medical devices such as the NC-stat System. During the second half of 2006 and in 2007, several local Medicare carriers issued draft LCDs, final LCDs or coding articles specifically addressing coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System or other automated nerve conduction equipment. Several of these carriers indicated that they will not reimburse physicians under Medicare for nerve conduction studies performed using the NC-stat System under the three existing Current Procedural Terminology, or CPT, codes for conventional nerve conduction studies (95900, 95903 and 95904) but rather that physicians must submit claims for reimbursement for these procedures under a miscellaneous CPT code (95999), in which case the local carriers may determine the level of reimbursement to be paid, if any. CPT codes are used in the submission of claims to insurers, including the Center for Medicaid and Medicare Services, for reimbursement for medical services. CPT codes are assigned, maintained and revised by the CPT Editorial Panel administered by the AMA. There are three local Medicare carriers with final LCDs, one local Medicare carrier with a draft LCD, and one local Medicare carrier with a coding article which address coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System. One additional Medicare carrier, which had previously issued a final LCD, reversed their position effective June 30, 2007. In certain regions impacted by these reimbursement decisions, our customers have experienced lower levels of reimbursement and higher levels of claims denials. If physicians do not receive adequate reimbursement under the miscellaneous CPT code from those local carriers, our existing customers may continue to limit or curtail their use of

the NC-stat System and we may be unable to obtain new customers, both of which could materially and adversely impact our revenues and profitability.

The AMA formed a work group in early 2007 to examine the reimbursement coding of nerve conduction studies and nerve conduction equipment, including the NC-stat System. The findings of this committee were presented to the AMA CPT Editorial Panel at a meeting in February 2008. During the CPT Panel meeting, several proposals for new Category I CPT codes, which generally are included in the Medicare physician fee schedule and are assigned specified reimbursement values, were presented by the chairpersons of the work group and were supported by several physician societies. In spite of this, the only proposal voted on was for the creation of a new Category III CPT code, which generally would not be included on the Medicare physician fee schedule and would not generally have an assigned reimbursement value, for nerve conduction studies performed using equipment with certain automated features such as the NC-stat System. At this meeting, we believe that the CPT Panel approved a new Category III CPT Code for nerve conduction studies performed using equipment with certain automated features such as the NC-stat System. Unless we are able to successfully challenge this decision, a new Category III CPT Code would likely be published in July 2008 and become effective in January 2009. In the event that a Category III CPT code is published which describes nerve conduction studies performed with the NC-stat System, it would likely result in limited or no Medicare reimbursement for such studies as a result of the potential that no specified reimbursement values would be assigned to these codes. This is likely to adversely impact reimbursement by other third party payers and is likely to have an adverse and material impact on our revenues and results of operations.

The LCDs and coding articles issued by local Medicare carriers have also addressed a number of other issues, including (1) the background and training of physicians supervising or performing nerve conduction studies, (2) the level of training requirements for technicians performing a nerve conduction study, (3) whether nerve conduction tests should be required to be performed concomitantly with a needle electromyography procedure and (4) whether the NC-stat System is comparable to conventional nerve conduction testing equipment. We do not believe that these LCDs prohibit physicians from receiving reimbursement under Medicare for medically necessary nerve conduction studies performed using the NC-stat System. However, these LCDs do appear to be targeted at limiting access to perform and/or reimbursement for nerve conduction studies. In certain cases, these LCDs are being interpreted or implemented in a manner that impacts the ability of physicians to receive reimbursement under Medicare, including lower levels of reimbursement and an increase in the number of claims being denied, for nerve conduction studies performed using the NC-stat System, which is having an adverse impact on our revenues.

Additionally, a significant number of commercial payers, including the majority of regional Blue Cross Blue Shield carriers, and other major private payers, have adopted general policies indicating that they will not provide reimbursement for the use of the NC-stat System. These general policies are not followed in every situation, and may be impacted by other factors such as specific arrangements with insured persons or physicians and any local or regional policies these payers have in place; however, we believe these general policies are negatively impacting the use of the NC-stat System by existing customers and our sales to new customers, both of which are having an adverse impact on our revenues. These commercial payers have cited various reasons for their reimbursement policies, including, among others, that the NC-stat System is experimental and investigational. We have been communicating with these payers, directly, through our customers or through our network of reimbursement consultants, to attempt to address their concerns. Third-party payers may also impose requirements on physicians to submit additional paperwork supporting the medical necessity of nerve conduction studies performed using the NC-stat System. We believe these requirements are negatively impacting the use of the NC-stat System by existing customers and our sales to new customers, both of which are having an adverse impact on our revenues.

Additional third-party payers, including local Medicare carriers and commercial payers, could potentially take a position that could reduce or eliminate the reimbursement for the NC-stat System and could have the impact of deterring usage by our customers and could have an adverse impact on our revenues.

We believe that eye scans performed using the DigiScope are being reimbursed by the majority of third-party payers. Many commercial payers have policies in place providing for reimbursement for the use of the DigiScope and many of these payers have published favorable articles about the DigiScope in their newsletters. However, several Medicare carriers have issued draft LCDs and coding articles that require a diagnosis of pre-existing retinal disease and/or will only reimburse for fundus photography, a highly specialized form of medical imaging, when performed in conjunction with an eye examination performed by an eye specialist. There are no assurances that other Medicare carriers will not issue similar draft LCDs, final LCDs or coding articles restricting the reimbursement for the use of the DigiScope. We believe that eye examinations performed on patients covered by Medicare represented less than 25% of our DigiScope revenues in 2007. However, the restrictions on reimbursement by Medicare carriers could have an adverse impact on our ability to grow our DigiScope revenues in future periods.

In the optometry clinic market, we may not be as dependent on reimbursement by third parties since many of the screenings performed in these clinics using the DigiScope are paid for by patients out of pocket. The more comprehensive tests performed in the optometry clinics using the DigiScope are submitted for reimbursement and our ability to penetrate this market and grow our revenues will be dependent on favorable reimbursement from third-party payers.

In the United States, some insured individuals are receiving their medical care through managed care programs, which monitor and often require pre-approval of the services that a member will receive. Some managed care programs are paying their providers on a per capita basis, which puts the providers at financial risk for the services provided to their patients by paying these providers a predetermined payment per member per month, and consequently, may limit the willingness of these providers to use our products.

We believe that the overall escalating cost of medical products and services has led to, and will continue to lead to, increased pressures on the healthcare industry to reduce the costs of products and services. We cannot assure you that third-party reimbursement and coverage will be available or adequate, or that future legislation, regulation, or reimbursement policies of third-party payers will not adversely affect the demand for our products or our ability to sell these products on a profitable basis. The unavailability or inadequacy of third-party payer coverage or reimbursement could have a material adverse effect on our business, operating results and financial condition. In addition, we believe that pressure is being applied on payer organizations by specialists, such as neurologists, who perform traditional nerve conduction studies and view the NC-stat System as competitive with their business.

FDA and Other Governmental Regulation

FDA Regulation

Our products are medical devices subject to extensive regulation by the FDA under the U.S. Federal Food, Drug, and Cosmetic Act, or FDCA, and the regulations promulgated thereto, as well as other regulatory bodies in the U.S. and abroad. The FDA classifies medical devices into one of three classes on the basis of the controls deemed necessary to reasonably ensure their safety and effectiveness:

Class I, requiring general controls, including labeling, device listing, reporting and, for some products, adherence to good manufacturing practices through the FDA's quality system regulations and pre-market notification;

Class II, requiring general controls and special controls, which may include performance standards and post-market surveillance; and

Class III, requiring general controls and PMA, which may include post-approval conditions and post-market surveillance.

Before being introduced into the market, our products must obtain market clearance or approval through the 510(k) pre-market notification process, the *de novo* review process or the PMA process.

510(k) Pre-Market Notification Process

To obtain 510(k) clearance, we must submit a pre-market notification demonstrating that the proposed device is substantially equivalent in intended use, safety and effectiveness to a legally marketed Class I or II medical device or to a Class III device marketed prior to May 28, 1976 for which the FDA has not yet required the submission of a PMA application. In some cases, we may be required to perform clinical trials to support a claim of substantial equivalence. If clinical trials are required, we must submit an application for an investigational device exemption, or IDE, which must be cleared by the FDA prior to the start of a clinical investigation, unless the device and clinical investigation are considered non-significant risk by the FDA or are exempt from the IDE requirements. It generally takes three months from the date of the pre-market notification submission to obtain 510(k) clearance, but it can be significantly longer.

After a medical device receives 510(k) clearance, any modification that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, requires a new 510(k) clearance or could require *de novo* classification or PMA. The FDA allows each company to make this determination, but the FDA can review the decision. If the FDA disagrees with a company's decision not to seek FDA authorization, the FDA may require the company to seek 510(k) clearance or PMA. The FDA also can require the company to cease marketing and/or recall the medical device in question until 510(k) clearance, *de novo* classification or PMA is obtained or take other action.

De Novo Review Process

If a previously unclassified medical device does not qualify for the 510(k) pre-market notification process because there is no predicate device to which it is substantially equivalent, and if the device may be adequately regulated through general controls or special controls, the device may be eligible for *de novo* classification through what is called the *de novo* review process. In order to use the *de novo* review process, a company must receive a letter from the FDA stating that, because the device has been found not substantially equivalent to a legally marketed Class I or II medical device or to a Class III device marketed prior to May 28, 1976 for which the FDA has not yet required the submission of a PMA application, it has been placed into Class III. After receiving this letter, the company, within 30 days, must submit to the FDA a request for *de novo* classification into Class I or II. The FDA then has 60 days in which to classify the device. If the FDA grants *de novo* classification, the device will be placed into either Class I or Class II, and allowed to be marketed. If a product is classified into Class I or II through the *de novo* review process, then that device may serve as a predicate device for subsequent 510(k) pre-market notifications.

PMA Process

If a medical device does not qualify for the 510(k) pre-market notification process and is not eligible for clearance through the *de novo* review process, a company must file a PMA application. The PMA process generally requires more extensive pre-filing testing than is required in the 510(k) pre-market notification process and is more costly, lengthy and uncertain. The PMA process can take one to three years or longer, from the time the PMA application is filed with the FDA. The PMA process requires the company to prove that there is a reasonable assurance of the safety and

effectiveness of the device to the FDA's satisfaction through extensive submissions, including pre-clinical and clinical trial data, and information about the device, its design, manufacture, labeling and components. Before granting PMA, the FDA generally also performs an on-site inspection of manufacturing facilities for the product to ensure compliance with the FDA's quality system regulations.

If FDA grants PMA, the approved indications may be more limited than those originally sought. In addition, FDA's approval order may include post-approval conditions that the FDA believes necessary to ensure the safety and effectiveness of the device, including, among other things, restrictions on labeling, promotion, sale and distribution and post-market study requirements. Failure to comply with the post-approval conditions can result in adverse enforcement or administrative actions, including the withdrawal of the approval. After any PMA, a new PMA application or application supplement may be required in the event of modifications to the device, its labeling, intended use or indication, or its manufacturing process that affect safety and effectiveness.

Post-Approval Obligations

After a device is placed on the market, numerous regulatory requirements continue to apply. These include:

- the FDA's Quality System Regulation, or QSR, which requires manufacturers, including third-party manufacturers, to follow stringent design, testing, control, documentation and other quality assurance procedures during all aspects of the manufacturing process;

- labeling regulations and FDA prohibitions against the promotion of products for uncleared or unapproved uses (known as off-label uses), as well as requirements to provide adequate information on both risks and benefits;

- medical device reporting, or MDR, regulations, which require that manufacturers report to FDA if their device may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a death or serious injury if the malfunction were to recur;

- correction and removal reporting regulations, which require that manufacturers report to the FDA field corrections and device recalls or removals if undertaken to reduce a risk to health posed by the device or to remedy a violation of the FDCA caused by the device which may present a risk to health;

- post-market surveillance regulations, which apply to Class II or III devices if the FDA has issued a post-market surveillance order and the failure of the device would be reasonably likely to have serious adverse health consequences, the device is expected to have significant use in the pediatric population, the device is intended to be implanted in the human body for more than one year, or the device is intended to be used to support or sustain life and to be used outside a user facility;

- regular and for cause inspections by FDA to review a manufacturer's facilities and their compliance with applicable FDA requirements; and

- the FDA's recall authority, whereby it can ask, or order, device manufacturers to recall from the market a product that is in violation of governing laws and regulations.

NC-stat System

The NC-stat System has received six 510(k) clearances as a Class II medical device, the first of which was received in 1998, and the most recent (K060584) in July 2006. The NC-stat System has the following intended use, as stated in the most recent 510(k) clearance:

> *"The NeuroMetrix NC-stat is intended to stimulate and measure neuromuscular signals that are useful in diagnosing and evaluating systemic and entrapment neuropathies."*

We believe that this intended use is consistent with the manner in which the NC-stat System is marketed and used by our customers.

As noted above, during the fourth quarter of 2006, at the request of the FDA, we submitted a 510(k) filing relating to portions of the onCall Information System that are currently in use. We are currently in the process of responding to the second additional information request that we have received from the FDA relating to this filing. During the first quarter of 2007, we also submitted a 510(k) for the ADVANCE System, which is also pending review by the FDA.

DigiScope

The DigiScope received a 510(k) clearance (K990205) as a Class II medical device in March 1999 and the indications for use statement is as follows:

> *"The DigiScope is indicated for use as an ophthalmic camera for individuals where examination of the fundus for pathologies is requested."*

Manufacturing Facilities

The facilities utilized by Parlex and Sunburst, two of our contract manufacturers, to supply our products have each been inspected by FDA in the past, and observations were noted. There were no findings that involved a significant violation of regulatory requirements. The responses to these observations have been accepted by FDA, and we believe that we are in substantial compliance with the QSR. Like all manufacturers, we expect our contract manufacturers to be inspected by FDA again in the future. If FDA finds significant violations, we could be subject to fines, recalls, requirements to halt manufacturing or other administrative or judicial sanctions. TopZone, our contract manufacturer for the DigiScope in China, has not been inspected by the FDA.

U.S. Anti-Kickback and False Claims Laws

In the United States, there are federal and state anti-kickback laws that prohibit the offer, payment, solicitation or receipt of kickbacks, bribes or other remuneration, whether direct or indirect, overt or covert, in cash or in kind, intended, among other things, to induce the purchase or recommendation of healthcare products and services. While the federal law applies only to products and services for which payment may be made by a federal healthcare program, the state laws may apply regardless of whether any public healthcare funds are involved. Violations of these laws can lead to severe civil and criminal penalties, including exclusion from participation in federal healthcare programs. These laws are potentially applicable to manufacturers of medical devices, such as us, and to hospitals, physicians and other potential purchasers of medical devices. Other provisions of state and federal law provide civil and criminal penalties for presenting, or causing to be presented, to third-party payers for reimbursement, claims that are false or fraudulent, or which are for items or services that were not provided as claimed. Under the federal civil False Claims Act, in addition to actions initiated by federal law enforcement authorities, the statute authorizes "qui tam" actions to be brought on behalf of the federal government by a private party in certain circumstances and, if successful, that private party can share in any monetary recovery. Any challenge by federal or state enforcement officials or others under these laws, including the current investigation by the Office of Inspector

General, or OIG, within the Department of Health and Human Services and by the United States Department of Justice, or DOJ, could have a material adverse effect on our business, financial condition and results of operations. As described in more detail in the section titled "Legal Proceedings," we are currently subject to investigations by the OIG and the DOJ of various aspects of our practices related to the NC-stat System.

Employees

As of December 31, 2007, we had a total of 143 employees. Of the total employees, 33 were in research and development, 75 in sales and marketing and 35 in general and administrative services. One employee holds both M.D. and Ph.D. degrees, six additional employees hold Ph.D. degrees and one additional employee holds an M.D. degree.

Our employees are not represented by a labor union and are not subject to a collective bargaining agreement. We have never experienced a work stoppage. We believe our relations with our employees are good.

Available Information

We were organized as a corporation in the state of Delaware in 1996. Access to our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to these reports filed with or furnished to the Securities and Exchange Commission, or SEC, may be obtained through the Investor Relations section of our website at www.neurometrix.com/investor as soon as reasonably practical after we electronically file or furnish these reports. We do not charge for access to and viewing of these reports. Information on our Investor Relations page and on our website is not part of this Annual Report on Form 10-K or any of our other securities filings unless specifically incorporated herein by reference. In addition, the public may read and copy any materials that we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Also, our filings with the SEC may be accessed through the SEC's Electronic Data Gathering, Analysis and Retrieval system at www.sec.gov. All statements made in any of our securities filings, including all forward-looking statements or information, are made as of the date of the document in which the statement is included, and we do not assume or undertake any obligation to update any of those statements or documents unless we are required to do so by law.

ITEM 1A. Risk Factors

You should carefully consider the following risks and all other information contained in this Annual Report on Form 10-K and our other public filings before making any investment decisions with respect to our common stock. If any of the following risks occurs, our business, prospects, reputation, results of operations or financial condition could be harmed. In that case, the trading price of our common stock could decline, and our stockholders could lose all or part of their investment. This Annual Report also contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of specific factors, including the risks described below and elsewhere in this Annual Report.

We have incurred significant operating losses since inception and cannot assure you that we will again achieve profitability.

The extent of our future operating income or losses is highly uncertain, and we may not be able to reach and sustain profitability. We have incurred significant cumulative net losses since our inception, including net losses of approximately $3.9 million in 2003 and $4.7 million in 2004. In 2005 and 2006, we recorded net income of approximately $249,000 and $4.3 million, respectively. However, we incurred a net loss of approximately $8.4 million in 2007 as a result of a decline in revenues and increases in operating expenses. At December 31, 2007, we had an accumulated deficit of approximately $62.1 million. We cannot assure you that we will be able to reach profitability again and sustain profitability.

If physicians or other healthcare providers are unable to obtain sufficient reimbursement from third-party healthcare payers for procedures performed using our products, the adoption of our products and our future product sales will be severely harmed.

Widespread adoption of our products by the medical community is unlikely to occur if physicians do not receive sufficient reimbursement from third-party payers for performing procedures using our products. If physicians are unable to obtain adequate reimbursement for procedures performed using our products, we may be unable to sell our products and our business would suffer significantly. Additionally, even if these procedures are reimbursed by third-party payers, adverse changes in payers' policies toward reimbursement for the procedures would harm our ability to market and sell our products. Third-party payers include those governmental programs such as Medicare and Medicaid, workers' compensation programs, private health insurers and other organizations. These organizations may deny coverage if they determine that a procedure was not reasonable or necessary, for example, if its use was not considered medically appropriate, or was experimental, or was performed for an unapproved indication. In addition, some health care systems are moving towards managed care arrangements in which they contract to provide comprehensive healthcare for a fixed cost per person, irrespective of the amount of care actually provided. These providers, in an effort to control healthcare costs, are increasingly challenging the prices charged for medical products and services and, in some instances, have pressured medical suppliers to lower their prices. If we are pressured to lower our prices, our revenues may decline and our profitability could be harmed. CMS guidelines set the reimbursement rates for procedures covered by Medicare. Future regulatory action by CMS or other governmental agencies or negative clinical results may diminish reimbursement payments to physicians for performing procedures using our products. Medicaid reimbursement differs from state to state, and some state Medicaid programs may not reimburse physicians for performing procedures using our products in an adequate amount, if at all. Additionally, some private payers do not follow the CMS and Medicaid guidelines and may reimburse for only a portion of these procedures or not at all. We are unable to predict what changes will be made in the reimbursement methods used by private or governmental third-party payers.

During the second half of 2006 and in 2007, several local Medicare carriers issued draft LCDs, final LCDs or coding articles particularly addressing coverage and reimbursement policies under

Medicare for nerve conduction studies performed using the NC-stat System. Several of these carriers indicated that they will not reimburse physicians under Medicare for nerve conduction studies performed using the NC-stat System under the three existing Current Procedural Terminology, or CPT, codes for conventional nerve conduction studies (95900, 95903 and 95904), which provide for levels of reimbursement fixed by the Center for Medicaid and Medicare Services, or CMS, but rather that physicians must submit claims for reimbursement for these procedures under a miscellaneous CPT code (95999), in which case the local carriers may determine the level of reimbursement to be paid, if any. Currently, there are three local Medicare carriers with final LCDs, one local Medicare carrier with a draft LCD, and one local Medicare carrier with a coding article which address coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System. One additional Medicare carrier, which had previously issued a final LCD, reversed their position effective June 30, 2007. In certain regions impacted by these reimbursement decisions, our customers have experienced lower levels of reimbursement and higher levels of claims denials. If physicians do not receive adequate reimbursement under the miscellaneous CPT code from those local carriers, our existing customers may continue to limit or curtail their use of the NC-stat System and we may be unable to obtain new customers, both of which could materially and adversely impact our revenues and profitability.

The AMA formed a work group in early 2007 to examine the reimbursement coding of nerve conduction studies and nerve conduction equipment, including the NC-stat System. The findings of this committee were presented to the AMA CPT Editorial Panel at a meeting in February 2008. During the CPT Panel meeting, several proposals for new Category I CPT codes, which generally are included in the Medicare physician fee schedule and are assigned specified reimbursement values, were presented by the chairpersons of the work group and were supported by several physician societies. In spite of this, the only proposal voted on was for the creation of a new Category III CPT code, which generally would not be included on the Medicare physician fee schedule and would not generally have an assigned reimbursement value. At this meeting, we believe that the CPT Panel approved a new Category III CPT Code for nerve conduction studies performed using equipment with certain automated features such as the NC-stat System. Unless we are able to successfully challenge this decision, a new Category III CPT Code would likely be published in July 2008 and become effective in January 2009. In the event that a Category III CPT code is published which describes nerve conduction studies performed with the NC-stat System, it would likely result in limited or no Medicare reimbursement for such studies as a result of the potential that no specified reimbursement values would be assigned to these codes. This could also adversely impact reimbursement by other third party payers and could have an adverse and material impact on our revenues and results of operations.

The LCDs and coding articles issued by local Medicare carriers have also addressed a number of other issues, including (1) the background and training of physicians supervising or performing nerve conduction studies, (2) the level of training requirements for technicians performing a nerve conduction study, (3) whether nerve conduction tests should be required to be performed concomitantly with a needle electromyography procedure and (4) whether the NC-stat System is comparable to conventional nerve conduction testing equipment. We do not believe that these LCDs prohibit physicians from receiving reimbursement under Medicare for medically necessary nerve conduction studies performed using the NC-stat System. However, these LCDs do appear to be targeted at limiting access to perform and/or reimbursement for nerve conduction studies. In certain cases, these LCDs are being interpreted or implemented in a manner that impacts the ability of physicians to receive reimbursement under Medicare, including lower levels of reimbursement and an increase in the number of claims being denied, for nerve conduction studies performed using the NC-stat System, which are having an adverse impact on our revenues.

Additionally, a significant number of commercial payers, including the majority of regional Blue Cross Blue Shield carriers, and other major private payers, have adopted policies indicating that they will not provide reimbursement for the use of the NC-stat System. These commercial payers have cited

various reasons for their reimbursement policies, including, among others, that the NC-stat System is experimental and investigational. We are in the process of communicating with these payers, directly, through our customers or through our network of reimbursement consultants, to attempt to address their concerns. Third-party payers may also impose requirements on physicians to submit additional paperwork supporting the medical necessity of nerve conduction studies performed using the NC-stat System. We believe these requirements are negatively impacting the use of the NC-stat System by existing customers and our sales to new customers, both of which are having an adverse impact on our revenues.

Additional third-party payers, including local Medicare carriers and commercial payers, could potentially take a position that could reduce or eliminate the reimbursement for the NC-stat System and could have the impact of deterring usage by our customers and could have an adverse impact on our revenues.

If physicians do not receive access to and adequate reimbursement under the miscellaneous CPT code from those local carriers that currently, or in the future, require procedures performed using the NC-stat System to be submitted using that code, or if the AMA publishes a Category III CPT code for nerve conduction studies performed using equipment such as the NC-stat System, our existing customers may limit or curtail their use of the NC-stat System, we may be unable to obtain new customers and we may face increasing pricing pressure, all of which could materially adversely impact our business and our revenues and profitability, in particular. If the LCDs recently adopted or reimbursement determinations adopted in the future relating to the reimbursement of nerve conduction studies place additional restrictions or qualifications on the performance of these procedures generally or using the NC-stat System, our business, revenues and profitability could be materially adversely affected. Additionally, in the short-term, the uncertainty caused by these recent changes, or other future changes, in third-party payers' reimbursement policies regarding nerve conduction studies may cause existing customers to reduce their use of the NC-stat System and potential new customers to defer a decision or decline to purchase the NC-stat System, which could materially adversely affect our business. We are expending and anticipate continuing to expend substantial resources to address potential reimbursement issues with third-party payers. Widespread adoption of the NC-stat System by the medical community is unlikely to occur if physicians do not receive satisfactory reimbursement from third-party payers for procedures performed with the NC-stat System.

Many Medicare regions, including those accounting for 30 of the 50 states, allow examinations using the DigiScope to be reimbursed on the basis of a general diabetes diagnosis. All or part of six states require a diagnosis of pre-existing retinal disease before reimbursement for an examination using the DigiScope and another six states will only reimburse for fundus photography when performed in conjunction with an eye exam performed by an ophthalmologist or optometrist. Of the latter, a Medicare carrier for four of the six states issued informal directives curtailing reimbursement in the second quarter of 2007. Also during this period, regional Medicare carriers covering all or parts of nine other states issued proposed LCDs indicating that they would only reimburse for retinal photography, including "telescreening," when performed concurrently with a personal examination by an ophthalmologist or optometrist and that digital imaging systems used for the detection of diabetic retinopathy, which acquire images and transmit them to a remote area for interpretation, are considered screening and do not meet Medicare's reasonable and necessary criteria for reimbursement. Although this decision does not have a material impact on our current business, we can offer no assurance that other Medicare carriers will not propose and adopt similar no coverage decisions.

We may be unable to expand the market for the NC-stat System, which would limit our ability to increase our revenues.

We believe that the drawbacks of traditional nerve conduction studies, including those related to the referral process, and the limited treatment options for DPN, have limited the number of nerve conduction studies that are performed. For our future growth, we are relying, in part, on increased use

of nerve conduction studies. A number of factors could limit the increased use of nerve conduction studies and the NC-stat System, including:

- third-party payers challenging, or the threat of third-party payers challenging, the necessity of increased levels of nerve conduction studies;
- third-party payers reducing or eliminating reimbursement for procedures performed by physicians using the NC-stat System;
- unfavorable experiences by physicians using the NC-stat System;
- physicians' reluctance to alter their existing practices; and
- the failure of other companies' existing drug development programs to produce an effective treatment for DPN, which may limit the perceived need and the actual use of the NC-stat System in connection with this disease, and thereby limit or delay our growth in the DPN market, which we have estimated to be our largest potential market for our NC-stat System.

If we are unable to expand the market for the NC-stat System, our ability to increase our revenues will be limited and our business prospects will be adversely affected.

Under-utilization of the DigiScope by customers may negatively affect our cash flow and potential profitability.

We lease our DigiScopes to our customers and retain title to the device. We generate revenues through an initial installation fee, ongoing rental fees and per patient examination fees. As such, we are responsible for all the costs of DigiScopes placed with our customers and a significant portion of our recovery of these costs takes place over time as we collect rental and per patient fees. If our customers fail to utilize or under-utilize the DigiScopes, we may not be able to recover all of our production costs and our cash flow and potential profitability will be negatively affected.

We may not be able to accurately predict the size of the market for our products.

We may not be able to accurately predict the size of the market for our products. Neuropathies traditionally have been diagnosed by an NCS/nEMG procedure, performed by a neurologist or physician in a related specialty. We estimate that there are approximately 2.0 million traditional NCS/nEMG procedures performed each year in the United States. However, we anticipate that the advantages and increased availability of point-of-service nerve conduction product offerings could significantly increase the number of nerve conduction studies performed if satisfactory third-party reimbursement is available. Based on our analysis of current data, we estimate that the potential market size for point-of-service nerve conduction product offerings such as the NC-stat System in the diabetes, low back pain and CTS markets in the aggregate could be greater than 9.5 million annual patient tests. This represents a significant increase in the size of the market for nerve conduction studies and is based upon a number of assumptions and estimates, which themselves may not be accurate. For example, we have assumed that all initial office visits for low back pain may represent an opportunity for use of the NC-stat System, and we have estimated that an annual testing rate of 50% for all individuals diagnosed with diabetes represents the potential addressable market in diabetes. We estimate that the size of the market for a point-of-service product for the detection of diabetic retinopathy could be nearly $700 million. There are estimated to be 21 million people in the United States with diabetes and it is estimated that 15 million have actually been diagnosed with diabetes. Using an eye examination fee of $45 per patient, this represents a potential market size of nearly $700 million. Market size is difficult to predict, and we cannot assure you that our assumptions or estimates will prove to be correct. The industry and market data in this Annual Report on Form 10-K, on which we have based our assumptions and estimates of future market size, may be inaccurate or incomplete, and we have not independently verified those data. If our estimates of the sizes of the markets for our products is incorrect, our potential revenue growth may be limited.

If we are unable to successfully sell our products to primary care, specialist physicians and other healthcare providers, our ability to increase our revenues will be limited.

We are focusing our sales and marketing efforts for the NC-stat System on primary care and specialist physicians and the DigiScope on primary care physicians, endocrinologists and optometrists. As these physicians and other healthcare providers traditionally have not been targeted by companies selling equipment used to perform nerve conduction studies or eye scans, we may face difficulties in selling our products to them. Particularly, we may be unable to convince these physicians that our products provide effective alternatives or useful supplements to existing testing methods. In addition, these physicians may be reluctant to make the capital investment required to purchase the NC-stat System or use the DigiScope and alter their existing practices. If we are unable to successfully sell our products to primary care and specialist physicians, our ability to increase our revenues will be severely limited.

We are dependent on several single source manufacturers to produce the NC-stat System and the DigiScope and any changes in the relationships with these manufacturers could prevent us from delivering products to our customers in a timely manner and may adversely impact our future revenues or costs.

We rely on two third-party manufacturers to manufacture all of the components of the NC-stat System and one third-party manufacturer to produce all of the components of the DigiScope. In the event that our manufacturers cease to manufacture sufficient quantities of our products in a timely manner and on terms acceptable to us, we would be forced to locate alternate manufacturers. Additionally, if our manufacturers experience a failure in their production process, are unable to obtain sufficient quantities of the components necessary to manufacture our products or otherwise fail to meet our quality requirements, we may be forced to delay the manufacture and sale of our products or locate an alternative manufacturer. We may be unable to locate suitable alternative manufacturers for our products, particularly our NC-stat biosensors, for which the manufacturing process is relatively specialized, on terms acceptable to us, or at all. We have entered into an exclusive manufacturing and supply agreements with Parlex for the manufacture of the NC-stat biosensors, and Sunburst for the manufacture of our NC-stat monitors and docking stations. TopZone manufactures DigiScopes on a purchase order basis, rather than pursuant to a long-term contract. TopZone contracts with Xintian Fine Optical Instrument Corporation, or Xintian, in Guiyang, China for the optical head of the DigiScope, which is the most complex and important sub-component of the DigiScope. If Xintian were to fail to provide optical heads for the DigiScope production, we would be required to find alternative suppliers of optical heads. Since most of the components are standard off the shelf optical materials, we believe we could find alternative suppliers, but we could experience a temporary reduction in supply and an increase in cost for the DigiScope. In addition, we rely on TopZone to provide certain hardware and software development services. The loss of these services would likely delay and increase the cost of our research and development efforts.

In addition, because TopZone is organized and operates in China, we will be subject to business risks associated with foreign operations, including:

failure to fulfill Chinese regulatory requirements to manufacture DigiScopes or other future products;

adapting to the differing business practices and laws in China;

limited protection for intellectual property rights in China;

costs of enforcing contractual obligations in China;

political instability and unexpected changes in diplomatic and trade relationships;

currency exchange rate fluctuations; and

potentially adverse tax consequences.

We do occasionally experience transient inventory shortages on new products during the initial production ramp-up phase. If any of the changes in our relationships with these manufacturers as described above occurs, our ability to supply our customers will be severely limited until we are able to engage an alternate manufacturer or, if applicable, resolve any quality issues with our existing manufacturer. This situation could prevent us from delivering products to our customers in a timely manner, lead to decreased sales or increased costs, or harm our reputation with our customers.

If our manufacturers are unable to supply us with an adequate supply of products as we expand our markets, we could lose customers, our potential future growth could be limited and our business could be harmed.

In order for us to successfully expand our business within the United States and internationally, our contract manufacturers must be able to provide us with our products in substantial quantities, in compliance with regulatory requirements, in accordance with agreed upon specifications, at acceptable cost and on a timely basis. Our potential future growth could strain the ability of our manufacturers to deliver products and obtain materials and components in sufficient quantities. Manufacturers often experience difficulties in scaling up production, including problems with production yields and quality control and assurance. If we are unable to obtain sufficient quantities of high quality products to meet customer demand on a timely basis, we could lose customers, our growth may be limited and our business could be harmed.

We currently rely entirely on sales of the products that comprise the NC-stat System to generate a substantial portion of our revenues, and any factors that negatively impact our sales of these products could significantly reduce our ability to generate revenues.

We introduced the NC-stat System to the market in May 1999. We derive substantially all of our revenues from sales of the products that comprise the NC-stat System, and we expect that sales of these products will continue to constitute the majority of our sales for the foreseeable future. Accordingly, our ability to generate revenues is reliant on our ability to market and sell the products that comprise the NC-stat System, particularly the disposable biosensors, sales of which accounted for approximately 86-88% of our total revenues in each of the past three years. Our sales of these products may be negatively impacted by many factors, including:

changes in reimbursement rates or policies relating to our products by third-party payers;

decisions made by the AMA CPT Editorial Panel relating to the reimbursement of nerve conduction studies performed using the NC-stat System;

the failure of the market to accept our products;

manufacturing problems;

claims that our products infringe on patent rights or other intellectual property rights owned by other parties;

adverse regulatory or legal actions relating to our products;

competitive pricing and related factors; and

results of clinical studies relating to our products or our competitors' products.

If any of these events occurs, our ability to generate revenues could be significantly reduced.

The patent rights we rely upon to protect the intellectual property underlying our products may not be adequate, which could enable third parties to use our technology and would harm our ability to compete in the market.

Our success will depend in part on our ability to develop or acquire commercially valuable patent rights and to protect these rights adequately. Our patent position is generally uncertain and involves

complex legal and factual questions. The risks and uncertainties that we face with respect to our patents and other related rights include the following:

- the pending patent applications we have filed or to which we have exclusive rights may not result in issued patents or may take longer than we expect to result in issued patents;
- the claims of any patents that are issued may not provide meaningful protection;
- we may not be able to develop additional proprietary technologies that are patentable;
- other parties may challenge patents, patent claims or patent applications licensed or issued to us; and
- other companies may design around technologies we have patented, licensed or developed.

We also may not be able to protect our patent rights effectively in some foreign countries. For a variety of reasons, we may decide not to file for patent protection. Our patent rights underlying our products may not be adequate, and our competitors or customers may design around our proprietary technologies or independently develop similar or alternative technologies or products that are equal or superior to our technology and products without infringing on any of our patent rights. In addition, the patents licensed or issued to us may not provide a competitive advantage. If any of these events were to occur, our ability to compete in the market would be harmed.

We depend on a patent licensed to us by Johns Hopkins University as well as other contractual relationships with the Wilmer Eye Institute.

We possess our rights with respect to the patent underlying the DigiScope through a patent licensing agreement with Johns Hopkins University. The license agreement generally grants us exclusive rights with respect to the patent, subject to certain rights retained by Johns Hopkins University for non-profit research purposes. However, if we determine not to seek patent protection in any given country, Johns Hopkins University may seek patent protection and license any resulting patents to third parties or otherwise exploit such patents for its own exclusive benefit. Currently, we are the exclusive licensee with respect to patents issued in the United States, China, Indonesia, Australia, Israel, Hong Kong and Mexico. We have determined not to seek patent protection in Canada or the European Union, although Johns Hopkins University has agreed that nonetheless we may retain exclusive rights in those jurisdictions. Our decision not to seek patent protection in Canada and the European Union could negatively impact our ability to compete in those jurisdictions.

Under the license agreement, we are required to pay Johns Hopkins University royalties ranging from three to three and one-half percent of our net collected revenues, exclusive of installation fees, on a quarterly basis. In the event that we breach the licensing agreement, including as a result of the failure to make required royalty payments to Johns Hopkins University, or the failure to exercise commercially reasonable efforts to commercialize the technology, we could lose the licensing rights to the DigiScope technology.

Also, since Johns Hopkins University is an academic institution, our license agreement with it is subject to the federal Bayh-Dole Act, pursuant to which the federal government has certain limited rights to use the technology and even to require us to grant a license to one or more third parties if we are not fully developing the technology.

In addition to the licensing agreement, we have also entered into an agreement with the Wilmer Eye Institute at Johns Hopkins University pursuant to which the Wilmer Eye Institute receives digital scans from physicians using the DigiScope and eye specialists employed by the Wilmer Eye Institute analyze the images. Within 24-48 hours after receipt of the images, the eye specialists provide a report to the physician who performed the eye scan indicating the results of the scan. If the Wilmer Eye Institute could not continue to perform this service to our customers in a timely manner, our ability to generate revenues from the DigiScope could be adversely impacted.

We also may benefit from contractual relationships with Johns Hopkins University in the area of research and development. Johns Hopkins University conducts certain research projects, funded by outside sources, involving the DigiScope. We have contractual commitments to support these research projects and if results are positive, we may benefit indirectly from the studies and the publication of the results. However, it may be necessary in the future for us to increase our research and development budget to conduct ongoing or additional research.

Other rights and measures we have taken to protect our intellectual property may not be adequate, which would harm our ability to compete in the market.

In addition to patents, we rely on a combination of trade secrets, copyright and trademark laws, confidentiality, nondisclosure and assignment of invention agreements and other contractual provisions and technical measures to protect our intellectual property rights. In particular, we have sought no patent protection for the technology and algorithms we use in our onCall Information System and the technology and algorithms we use in connection with the DigiScope. We rely on trade secrets to protect this information. While we currently require employees, consultants and other third parties to enter into confidentiality, non-disclosure or assignment of invention agreements or a combination thereof where appropriate, any of the following could still occur:

- the agreements may be breached;
- we may have inadequate remedies for any breach;
- trade secrets and other proprietary information could be disclosed to our competitors; or
- others may independently develop substantially equivalent proprietary information and techniques or otherwise gain access to our trade secrets or disclose such technologies.

If, for any of the above reasons, our intellectual property is disclosed or misappropriated, it would harm our ability to protect our rights and our competitive position.

We may need to initiate lawsuits to protect or enforce our patents and other intellectual property rights, which could be expensive and, if we lose, could cause us to lose some of our intellectual property rights, which would harm our ability to compete in the market.

We rely on patents to protect a portion of our intellectual property and our competitive position. Patent law relating to the scope of claims in the technology fields in which we operate is still evolving and, consequently, patent positions in the medical device industry are generally uncertain. In order to protect or enforce our patent rights, we may initiate patent litigation against third parties, such as infringement suits or interference proceedings. Litigation may be necessary to:

- assert claims of infringement;
- enforce our patents;
- protect our trade secrets or know-how; or
- determine the enforceability, scope and validity of the proprietary rights of others.

Any lawsuits that we initiate could be expensive, take significant time and divert management's attention from other business concerns. Litigation also puts our patents at risk of being invalidated or interpreted narrowly and our patent applications at risk of not issuing. Additionally, we may provoke third parties to assert claims against us. We may not prevail in any lawsuits that we initiate and the damages or other remedies awarded, if any, may not be commercially valuable. The occurrence of any of these events could harm our business, our ability to compete in the market or our reputation.

Claims that our products infringe on the proprietary rights of others could adversely affect our ability to sell our products and increase our costs.

Substantial litigation over intellectual property rights exists in the medical device industry. We expect that our products could be increasingly subject to third-party infringement claims as the number of competitors grows and the functionality of products and technology in different industry segments overlap. Third parties may currently have, or may eventually be issued, patents on which our products or technologies may infringe. Any of these third parties might make a claim of infringement against us. Any litigation regardless of its impact would likely result in the expenditure of significant financial resources and the diversion of management's time and resources. In addition, litigation in which we are accused of infringement may cause negative publicity, adversely impact prospective customers, cause product shipment delays or require us to develop non-infringing technology, make substantial payments to third parties, or enter into royalty or license agreements, which may not be available on acceptable terms, or at all. If a successful claim of infringement were made against us and we could not develop non-infringing technology or license the infringed or similar technology on a timely and cost-effective basis, our revenues may decrease substantially and we could be exposed to significant liability.

We are subject to extensive regulation by the FDA, which could restrict the sales and marketing of the NC-stat System and could cause us to incur significant costs.

We sell medical devices that are subject to extensive regulation in the United States by the FDA for manufacturing, labeling, sale, promotion, distribution and shipping. Before a new medical device, or a new use of or claim for an existing product, can be marketed in the United States, it must first receive 510(k) clearance, grant of a *de novo* classification or pre-marketing approval from the FDA, unless an exemption applies. Medical devices may be marketed only for the indications for which they are approved or cleared. We may also be required to obtain a new 510(k) clearance or *de novo* classification or PMA for significant post-market modifications to our products including changes to the intended use. Each of these processes can be expensive and lengthy. The FDA's process for granting 510(k) clearance usually takes approximately three months, but it can be significantly longer. The process for obtaining *de novo* classification involves a level of scrutiny similar to the 510(k) clearance process, but may require more data. The process for obtaining PMA is much more costly and uncertain and it generally takes from one to three years, or longer, from the time the application is filed with the FDA.

Our clearances can be rescinded if safety or effectiveness problems develop. Further, we may not be able to obtain additional 510(k) clearances or premarket approvals for new products or for modifications to, or additional indications for, our existing products in a timely fashion, or at all. Delays in obtaining future clearances or approvals would adversely affect our ability to introduce new or enhanced products in a timely manner, which in turn would harm our revenue and future profitability. We have made modifications to our devices in the past and may make additional modifications in the future that we believe do not or will not require additional clearances or approvals. If the FDA disagrees, and requires new clearances or approvals for the modifications, we may be required to recall and to stop marketing the modified devices. If any of these events occur or if the FDA takes other administrative or judicial actions, we may not be able to provide our customers with the quantity of products they require on a timely basis, our reputation could be harmed, and we could lose customers and suffer reduced revenues and increased costs. In particular, our business could be adversely impacted in the event that we do not obtain 510(k) clearance for the ADVANCE System or the portions of the onCall Information System that are the subject of our 510(k) filing in the fourth quarter of 2006. Because the portions of the onCall Information System under review are currently in use, if the FDA does not clear them, we may be required to modify or remove the portions of the onCall Information System that are under review. Any such modifications could make the NC-stat System more difficult to use by physicians, which could adversely impact our ability to generate revenues from

the NC-stat System, or more expensive for us to operate. Either of these could have a material adverse impact on our business.

We also are subject to numerous post-marketing regulatory requirements, including quality system regulations, which relate to the design, manufacture, packaging, labeling, storage, installation and servicing of our products, labeling regulations, medical device reporting regulations and correction and removal reporting regulations. Our failure or the failure by any manufacturer of our products to comply with applicable regulatory requirements could result in enforcement action by the FDA, which may include any of the following sanctions:

- warning letters, fines, injunctions, product seizures, consent decrees and civil penalties;
- requiring repair, replacement, refunds, notifications or recall of our products;
- imposing operating restrictions, suspension or shutdown of production;
- refusing our requests for 510(k) clearance or PMA of new products, new intended uses, or modifications to existing products;
- rescinding 510(k) clearances or withdrawing PMAs that have already been granted; and
- criminal prosecution.

If any of these events were to occur, they could harm our reputation, our ability to generate revenues and our profitability.

Also, from time to time, legislation is introduced into Congress that could significantly change the statutory provisions governing the approval, manufacturing and marketing of medical devices. In addition, FDA regulations and guidance are often revised or reinterpreted by the agency in ways that may significantly affect our business and our products. It is impossible to predict whether legislative changes will be enacted, or FDA regulations, guidance or interpretations changed, and what the impact of such changes, if any, may be.

If we or the manufacturers of our products fail to comply with the FDA's quality system regulations, the manufacturing and distribution of our products could be interrupted, and our product sales and operating results could suffer.

We and our contract manufacturers are required to comply with the FDA's quality system regulations, which is a complex regulatory scheme that covers the procedures and documentation of the design, testing, production, control, quality assurance, labeling, packaging, sterilization, storage and shipping of our devices. The FDA enforces its quality system regulations through periodic inspections. We cannot assure you that our facilities or the facilities of the manufacturers of our products would pass any future quality system inspection. If our or any of the facilities of the manufacturers of our products fail a quality system inspection, the manufacturing or distribution of our products could be interrupted and our operations disrupted. Failure to take adequate and timely corrective action in response to an adverse quality system inspection could result in a suspension or shutdown of our packaging and labeling operations and the operations of the manufacturers of our products or a recall of our products, or other administrative or judicial sanctions. If any of these events occurs, we may not be able to provide our customers with the quantity of products they require on a timely basis, our reputation could be harmed, and we could lose customers and suffer reduced revenues and increased costs.

Our products may be subject to recalls even after receiving FDA clearance or approval, which would harm our reputation, business and financial results.

We are subject to the medical device reporting regulations, which require us to report to the FDA if our products may have caused or contributed to a death or serious injury, or have malfunctioned in a way that would likely cause or contribute to a death or serious injury if the malfunction were to occur. We are also subject to the correction and removal reporting regulations, which require us to report to the FDA any field corrections and device recalls or removals that we undertake to reduce a risk to health posed by the device or to remedy a violation of the FDCA caused by the device which may present a risk to health. In addition, the FDA and similar governmental bodies in other countries have the authority to require the recall of our products if there is a reasonable probability that the products would cause serious adverse health consequences or death. A government-mandated or voluntary recall by us could occur as a result of manufacturing defects, labeling deficiencies, packaging defects or other failures to comply with applicable regulations. Any recall would divert management attention and financial resources and harm our reputation with customers. A recall involving the NC-stat System would be particularly harmful to our business and financial results because the products that comprise the NC-stat System currently produce substantially all of our revenues.

We are subject to federal and state laws prohibiting "kickbacks" and false or fraudulent claims, which, if violated, could subject us to substantial penalties. Additionally, any challenge to or investigation into our practices under these laws could cause adverse publicity and be costly to respond to, and thus could harm our business.

A federal law commonly known as the Medicare/Medicaid anti-kickback law, and several similar state laws, prohibit any remuneration that is intended to induce physicians or others either to refer patients or to acquire or arrange for or recommend the acquisition of healthcare products or services. These laws constrain a medical device company's sales, marketing and other promotional activities by limiting the kinds of business relationships and financial arrangements, including sales programs we may have with hospitals, physicians or other potential purchasers of medical devices. Other federal and state laws generally prohibit individuals or entities from knowingly presenting, or causing to be presented, claims for payment to Medicare, Medicaid or other third-party payers that are false or fraudulent, or for items or services that were not provided as claimed. From time to time, we may provide coding and billing information as product support to purchasers of our products. Anti-kickback and false claims laws prescribe civil and criminal penalties for noncompliance, which can be quite substantial including exclusion from participation in federal healthcare programs. In the event that we are found to have violated these laws or determine to settle a claim that we have done so, our business may be materially adversely affected as a result of any payments required to be made, restrictions on our future operations or actions required to be taken, damage to our business reputation or adverse publicity in connection with such a finding or settlement or other adverse effects relating thereto. Additionally, even an unsuccessful challenge or investigation into our practices could cause adverse publicity, and be costly to respond to, and thus could harm our business and results of operations.

In the second quarter of 2006, we received a subpoena from the Office of Inspector General, or OIG, of the Department of Health and Human Services requesting documents from us in connection with an investigation of potential violations of the federal anti-kickback statute and False Claims Act. In addition, on June 21, 2007, we received a subpoena from the U.S. Attorney's Office for the District of Massachusetts requesting documents from us in connection with an investigation by the U.S. Department of Justice, or DOJ. We understand that the DOJ is investigating various aspects of our practices relating to the NC-stat System, including sales and marketing practices. We are cooperating with both investigations. During 2007, we formed a Special Committee of our Board of Directors to provide oversight of an ongoing independent review of our sales and marketing practices and of our continuing cooperation with the DOJ and OIG investigations. We cannot predict the ultimate outcome

of these investigations. We are unable to determine when these matters will be resolved, whether any additional areas of inquiry will be opened, or any outcome of this matter. Any negative findings in this matter could result in fines, penalties, or program exclusions, which could have a material adverse effect on our financial condition, results of operations and cash flows. We may also incur significant costs in responding to, and defending our company in these investigations, which could also have a material adverse effect on our financial condition, results of operations and cash flows.

If we are found to have violated laws protecting the confidentiality of patient health information, we could be subject to civil or criminal penalties, which could increase our liabilities and harm our reputation or our business.

There are a number of federal and state laws protecting the confidentiality of individually identifiable patient health information, including patient records, and restricting the use and disclosure of that protected information. In particular, the U.S. Department of Health and Human Services promulgated patient privacy rules under the Health Insurance Portability and Accountability Act of 1996, or HIPAA. These privacy rules protect medical records and other personal health information by limiting their use and disclosure, giving individuals the right to access, amend and seek accounting of their own health information and limiting most use and disclosures of health information to the minimum amount reasonably necessary to accomplish the intended purpose. Although we do not believe that we are subject to the HIPAA rules, the exact scope of these rules has not been clearly established. If we are found to be in violation of the privacy rules under HIPAA, we could be subject to civil or criminal penalties, which could increase our liabilities and harm our reputation or our business.

The use of our products could result in product liability claims that could be expensive, damage our reputation and harm our business.

Our business exposes us to an inherent risk of potential product liability claims related to the manufacturing, marketing and sale of medical devices. The medical device industry historically has been litigious, and we face financial exposure to product liability claims if the use of our products were to cause or contribute to injury or death. In particular, the NC-stat System may be susceptible to claims of injury because it involves the electric stimulation of a patient's nerves. Additionally, because the DigiScope tests for diabetic retinopathy, which is a condition that can lead to loss of vision or blindness if untreated, we could be subject to claims of injury relating to any actual or claimed inadequacy, error or malfunction of the DigiScope in testing for this condition or the Wilmer-EyeTel Reading Center in reading the results of the test performed by the DigiScope and communicating them to the physician. Although we maintain product liability insurance for our products and other commercial insurance, the coverage limits of these policies may not be adequate to cover future claims. As sales and use of our products increase, we may be unable to maintain sufficient product liability or other commercial insurance on acceptable terms or at reasonable costs, and this insurance may not provide us with adequate coverage against potential liabilities. A successful claim brought against us in excess of, or outside of, our insurance coverage could have a material adverse effect on our financial condition and results of operations. A product liability claim, regardless of its merit or eventual outcome, could result in substantial costs to us, a substantial diversion of management attention and adverse publicity. A product liability claim could also harm our reputation and result in a decline in revenues and an increase in expenses.

Our products are complex in design, and defects may not be discovered prior to shipment to customers, which could result in warranty obligations or product liability or other claims, reducing our revenues and increasing our costs and liabilities.

We depend upon third parties for the manufacture of our products. Our products, particularly our NC-stat biosensors, require a significant degree of technical expertise to produce. If these

manufacturers fail to produce our products to specification, or if the manufacturers use defective materials or workmanship in the manufacturing process, the reliability and performance of our products will be compromised.

If our products contain defects that cannot be repaired quickly, easily and inexpensively, we may experience:

loss of customer orders and delay in order fulfillment;

damage to our brand reputation;

increased cost of our warranty program due to product repair or replacement;

inability to attract new customers;

diversion of resources from our manufacturing and research and development departments into our service department; and

legal action.

The occurrence of any one or more of the foregoing could harm our reputation and materially reduce our revenues and increase our costs and liabilities.

If we lose any of our officers or key employees, our management and technical expertise could be weakened significantly.

Our success largely depends on the skills, experience and efforts of our officers, including Shai N. Gozani, M.D., Ph.D., our founder and President and Chief Executive Officer; Gary L. Gregory, our Chief Operating Officer; Guy Daniello, our Senior Vice President of Information Technology; Michael Williams, Ph.D., our Senior Vice President of Engineering; W. Bradford Smith, our Chief Financial Officer; and our other key employees. We maintain a $5.0 million key person life insurance policy on Dr. Gozani, for which the Company is the beneficiary, but do not maintain key person life insurance policies covering any of our other employees. The loss of any of our officers or key employees could weaken our management and technical expertise significantly and harm our business.

If we are unable to recruit, hire and retain skilled and experienced personnel, our ability to manage and expand our business will be harmed, which would impair our future revenues and profitability.

We are a small company with only 143 employees as of December 31, 2007, and our ability to retain our skilled labor force and our success in attracting and hiring new skilled employees will be a critical factor in determining our future performance. We may not be able to meet our future hiring needs or retain existing personnel, particularly given the challenges our business has recently faced. We will face challenges and risks in hiring, training, managing and retaining engineering and sales and marketing employees, as well as independent regional sales agencies and sales representatives, most of whom are geographically dispersed and must be trained in the use and benefits of our products. Failure to attract and retain personnel, particularly technical and sales and marketing personnel, would materially harm our ability to compete effectively and grow our business.

If we do not effectively manage our future potential growth, our business resources may become strained, we may not be able to deliver our products in a timely manner and our results of operations may be adversely affected.

Future potential growth of our business may provide challenges to our organization and may strain our management and operations. We may misjudge the amount of time or resources that will be required to effectively manage any anticipated or unanticipated growth in our business or we may not be able to attract, hire and retain sufficient personnel to meet our needs. If we cannot scale our

business appropriately, maintain control over expenses or otherwise adapt to anticipated and unanticipated growth, our business resources may become strained, we may not be able to deliver our products in a timely manner and our results of operations may be adversely affected.

If we are unable to successfully expand, develop and retain our sales force, our revenues may decline, our future revenue growth may be limited and our expenses may increase.

As of December 31, 2007, we employed approximately 50 regional sales managers, five regional sales directors and a national sales director. We are highly dependent on our regional sales managers to generate our revenues. Our ability to build and develop a strong sales force will be affected by a number of factors, including:

- our ability to attract, integrate and motivate sales personnel;
- our ability to effectively train our sales force;
- the ability of our sales force to sell an increased number of products;
- the length of time it takes new sales personnel to become productive;
- the competition we face from other companies in hiring and retaining sales personnel;
- our ability to effectively manage a multi-location sales organization;
- our ability to enter into agreements with prospective members of our sales force on commercially reasonable terms; and
- our ability to get our independent sales agencies, who may sell products of multiple companies, to commit the necessary resources to effectively market and sell our products.

If we are unable to successfully build, develop and retain a strong sales force, our revenues may decline, our revenue growth may be limited and our expenses may increase.

Failure to develop or enter into relationships to sell products other than our existing products or enhance our existing products could have an adverse effect on our business prospects.

For the year ended December 31, 2007, the majority of our revenues were derived from selling the NC-stat System. Our future business and financial success will depend, in part, on our ability to continue to introduce or sell new products and upgraded products into the marketplace. Developing new products and upgrades to existing and future products imposes burdens on our research and development department and our management. This process is costly, and we cannot assure you that we will be able to successfully develop new products or enhance the NC-stat System or any of our other current or future products. We also may not be able to enter into relationships with other companies to sell additional products. In addition, as we develop the market for our products, future competitors may develop desirable product features earlier than we do, which could make our competitors' products less expensive or more effective than our products and could render our products obsolete or unmarketable. If our product development efforts are unsuccessful, we will have incurred significant costs without recognizing the expected benefits and our business prospects may suffer.

We currently compete, and may in the future need to compete, against other medical device companies with potentially greater resources, more established distribution channels and other competitive advantages, and the success of these competitors may harm our ability to generate revenues.

We currently do, and in the future may need to, compete directly and indirectly with a number of other companies that enjoy significant competitive advantages over us. Currently, in the point-of-service market, we indirectly compete with companies that sell traditional NCS/nEMG equipment. In this market, these companies are indirect competitors because the equipment they sell traditionally has

41

been used by neurologists, who rely upon and seek to obtain referrals from primary care and specialist physicians to perform the same types of tests that may be performed by primary care and specialist physicians using the NC-stat System. Additionally, in selling the NC-stat System to neurologists, which is not a market we historically have focused on, we compete directly with the companies that sell traditional NCS/nEMG equipment. There are a number of companies that sell traditional NCS/nEMG equipment including Cardinal Healthcare, having acquired Viasys Healthcare Inc. in 2007, Cadwell Laboratories, Inc. and Natus, having acquired Xltec, Inc. in 2007. Additionally, we are aware of one company, Neumed, Inc., that markets a nerve conduction study system to the point-of-service market. Of these companies, Cardinal Healthcare, in particular, enjoys significant competitive advantages, including:

- greater resources for product development, sales and marketing;
- more established distribution networks;
- greater name recognition;
- more established relationships with health care professionals, customers and third-party payers; and
- additional lines of products and the ability to offer rebates or bundle products to offer discounts or incentives.

As we develop the market for point-of-service nerve conduction studies, we may be faced with competition from these companies or others that decide and are able to enter this market. Some or all of our future competitors in the point-of-service market may enjoy competitive advantages such as those described above. If we are unable to compete effectively against existing and future competitors, our sales will decline and our business will be harmed.

With respect to the DigiScope, our principal competitor in the primary diabetes care market is Veraxa Health, Inc., an affiliate of the Joslin Diabetes Center, and our principal competitors in the optometry market are Carl Zeiss, Inc., Topcon America Corporation, Kowa. Some or all of these existing competitors, as well as, future competitors may enjoy advantages, such as those described above relating to the nerve conduction market. If we are unable to compete effectively against existing and future competitors, our ability to grow our DigiScope revenues could be adversely impacted and our business could be harmed.

We are dependent upon the computer and communications infrastructure employed and utilized by our onCall Information System and the Wilmer EyeTel Reading Center, and any failures or disruptions in this infrastructure could impact our revenues and profit margins or harm our reputation.

We are dependent upon the computer and communications infrastructure employed and utilized by our onCall Information System and our DigiScopes. Our computer and communications infrastructure consists of standard hardware, off-the-shelf system software components, database servers, proprietary application servers, a modem bank and desktop applications. Our future success in selling the NC-stat System and the DigiScopes will depend, in part, upon the maintenance and growth of this infrastructure. Any failures or outages of this infrastructure as a result of a computer virus, intentional disruption of our systems by a third-party, manufacturing failure, telephone system failure, fire, storm, flood, power loss or other similar events, could prevent or delay the operation of our onCall Information System or the Wilmer EyeTel Reading Center, which could result in increased costs to eliminate these problems and address related security concerns and harm our reputation with our customers. In addition, if our infrastructure fails to accommodate growth in customer transactions, customer satisfaction could be impaired, we could lose customers, our ability to add customers could be impaired or our costs could be increased, any of which would harm our business.

If future clinical studies or other articles are published, or physician associations or other organizations announce positions, that are unfavorable to our products, our sales efforts and revenues may be negatively affected.

Future clinical studies or other articles regarding our existing products or any competing products may be published that either support a claim, or are perceived to support a claim, that a competitor's product is more accurate or effective than our products or that our products are not as accurate or effective as we claim or previous clinical studies have concluded. Additionally, physician associations or other organizations that may be viewed as authoritative or have an economic interest in nerve conduction studies and in related electrodiagnostic procedures or other procedures that may be performed using our products could endorse products or methods that compete with our products or otherwise announce positions that are unfavorable to our products. We have experienced this with the professional societies representing the neurologist community. Any of these events may negatively affect our sales efforts and result in decreased revenues.

Our future capital needs are uncertain and we may need to raise additional funds in the future, and these funds may not be available on acceptable terms or at all.

We believe that our current cash and cash equivalents together with our short-term investments and the cash to be generated from expected product sales will be sufficient to meet our projected operating requirements for at least the next 12 months. However, we may seek additional funds from public and private stock offerings, borrowings under credit lines or other sources. Our capital requirements will depend on many factors, including:

the revenues generated by sales of our products;

the costs associated with our sales and marketing efforts;

the expenses we incur in manufacturing and selling our products;

the costs of developing new products or technologies and enhancements to existing products;

the cost of obtaining and maintaining FDA approval or clearance of our products and products in development;

the costs associated with any expansion;

the costs of professional services associated with the government investigations to which we are subject;

the costs associated with capital expenditures, including the purchase of DigiScopes; and

the number and timing of any acquisitions or other strategic transactions.

As a result of these factors, we may need to raise additional funds, and these funds may not be available on favorable terms, or at all. Furthermore, if we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. In addition, if we raise additional funds through collaboration, licensing or other similar arrangements, it may be necessary to relinquish valuable rights to our potential products or proprietary technologies, or grant licenses on terms that are not favorable to us. If we cannot raise funds on acceptable terms, we may not be able to develop or enhance our products, execute our business plan, take advantage of future opportunities, or respond to competitive pressures or unanticipated customer requirements. If any of these events occurs, our ability to achieve our development and commercialization goals would be adversely affected.

If we choose to acquire or invest in new businesses, products or technologies, instead of developing them ourselves, these acquisitions or investments could disrupt our business and could result in the use of significant amounts of equity, cash or a combination of both.

From time to time we may seek to acquire or invest in businesses, products or technologies, instead of developing them ourselves. On December 26, 2007, for example, we acquired substantially all of the assets and assumed certain liabilities of EyeTel and in November 2007 we made an investment in Cyberkinetics and in 2008 entered into a joint venture with them.

Acquisitions and investments involve numerous risks, including:

- the inability to complete the acquisition or investment;
- disruption of our ongoing businesses and diversion of management attention;
- difficulties in integrating the acquired entities, products or technologies;
- difficulties in operating the acquired business profitably;
- the inability to achieve anticipated synergies, cost savings or growth;
- potential loss of key employees, particularly those of the acquired business;
- difficulties in transitioning and maintaining key customer, distributor and supplier relationships;
- risks associated with entering markets in which we have no or limited prior experience; and
- unanticipated costs.

In addition, any future acquisitions or investments may result in one or more of the following:

- issuances of dilutive equity securities, which may be sold at a discount to market price;
- the use of significant amounts of cash;
- the incurrence of debt;
- the assumption of significant liabilities;
- increased operating costs or reduced earnings;
- financing obtained on unfavorable terms;
- large one-time expenses; and

the creation of certain intangible assets, including goodwill, the write-down of which may result in significant charges to earnings.

Any of these factors could materially harm our stock price, our business or our operating results.

If we expand, or attempt to expand, into foreign markets, we will be affected by new business risks that may adversely impact our financial condition or results of operations.

We had our initial revenues in the United Kingdom in the third quarter of 2007, representing our initial launch in Europe. If we continue to expand, or attempt to expand, into foreign markets, we will be subject to new business risks, including:

failure to fulfill foreign regulatory requirements to market our products;

availability of, and changes in, reimbursement within prevailing foreign health care payment systems;

adapting to the differing business practices and laws in foreign countries;

difficulties in managing foreign relationships and operations, including any relationships that we establish with foreign distributors or sales or marketing agents;

limited protection for intellectual property rights in some countries;

difficulty in collecting accounts receivable and longer collection periods;

costs of enforcing contractual obligations in foreign jurisdictions;

recessions in economies outside of the United States;

political instability and unexpected changes in diplomatic and trade relationships;

currency exchange rate fluctuations; and

potentially adverse tax consequences.

If we are successful in introducing our products into foreign markets, we will be affected by these additional business risks, which may adversely impact our financial condition or results of operations. In addition, expansion into foreign markets imposes additional burdens on our executive and administrative personnel, research and sales departments, and general managerial resources. Our efforts to introduce our products into foreign markets may not be successful, in which case we may have expended significant resources without realizing the expected benefit. Ultimately, the investment required for expansion into foreign markets could exceed the revenues generated from this expansion.

Our operating results may fluctuate due to various factors and, as a result, period-to-period comparisons of our results of operations will not necessarily be meaningful.

Factors relating to our business make our future operating results uncertain and may cause them to fluctuate from period to period. These factors include:

changes in the availability of third-party reimbursement in the United States or other countries;

the timing of new product announcements and introductions by us or our competitors;

market acceptance of new or enhanced versions of our products;

changes in manufacturing costs or other expenses;

competitive pricing pressures;

the gain or loss of significant distribution outlets or customers;

increased research and development expenses;

the timing of any future acquisitions; or

general economic conditions.

Because our operating results may fluctuate from quarter to quarter, it may be difficult for us or our investors to predict our future performance by viewing our historical operating results.

Anti-takeover provisions in our organizational documents and Delaware law, and those anti-takeover provisions adopted by the Company in 2007, may discourage or prevent a change of control, even if an acquisition would be beneficial to our stockholders, which could affect our stock price adversely and prevent attempts by our stockholders to replace or remove our current management.

Our certificate of incorporation and bylaws contain provisions that could delay or prevent a change of control of our company or changes in our board of directors that our stockholders might consider favorable. Some of these provisions:

- authorize the issuance of preferred stock which can be created and issued by the board of directors without prior stockholder approval, with rights senior to those of our common stock;
- provide for a classified board of directors, with each director serving a staggered three-year term;
- prohibit our stockholders from filling board vacancies, calling special stockholder meetings, or taking action by written consent;
- provide for the removal of a director only with cause and by the affirmative vote of the holders of 75% or more of the shares then entitled to vote at an election of our directors; and
- require advance written notice of stockholder proposals and director nominations.

We have adopted a Shareholder Rights Plan that could make it more difficult for a third party to acquire, or could discourage a third party from acquiring, the Company or a large block of our common stock. A third party that acquires 15% or more of our common stock (an "acquiring person") could suffer substantial dilution of its ownership interest under the terms of the Shareholder Rights Plan through the issuance of common stock to all shareholders other than the acquiring person.

In addition, we are subject to the provisions of Section 203 of the Delaware General Corporation Law, which may prohibit certain business combinations with stockholders owning 15% or more of our outstanding voting stock. These and other provisions in our certificate of incorporation, bylaws and Delaware law could make it more difficult for stockholders or potential acquirers to obtain control of our board of directors or initiate actions that are opposed by our then-current board of directors, including a merger, tender offer, or proxy contest involving our company. Any delay or prevention of a change of control transaction or changes in our board of directors could cause the market price of our common stock to decline.

We do not intend to pay cash dividends.

We have never declared or paid cash dividends on our capital stock. We currently intend to retain all available funds and any future earnings for use in the operation and expansion of our business and do not anticipate paying any cash dividends in the foreseeable future. In addition, the terms of any future debt or credit facility may preclude us from paying any dividends. As a result, capital appreciation, if any, of our common stock will be our stockholders sole source of potential gain for the foreseeable future.

ITEM 1B. UNRESOLVED STAFF COMMENTS

We have not received written comments from the Securities and Exchange Commission regarding our periodic or current reports under the Securities and Exchange Act of 1934, as amended, 180 days or more before December 31, 2007 that remain unresolved.

ITEM 2. PROPERTIES

Our headquarters is located in a 30,000 square foot facility in Waltham, Massachusetts, which we occupy under an office lease expiring in March 2013. We also operate in a 13,700 square foot facility in Columbia, Maryland, leased to us until October 31, 2009. We believe that our existing facilities are adequate for our current needs.

ITEM 3. LEGAL PROCEEDINGS

In the second quarter of 2006, we received a subpoena from the Office of Inspector General, or OIG, of the Department of Health and Human Services requesting documents from us in connection with an investigation of potential violations of the federal anti-kickback statute and False Claims Act. In addition, on June 21, 2007, we received a subpoena from the U.S. Attorney's Office for the District of Massachusetts requesting documents from us in connection with an investigation by the DOJ. We understand that the DOJ is investigating various aspects of our practices relating to the NC-stat System, including sales and marketing practices. We are cooperating with both investigations. During 2007, we formed a Special Committee of our Board of Directors to provide oversight of an ongoing independent review of our sales and marketing practices and of our continuing cooperation with the DOJ and OIG investigations. We cannot predict the ultimate outcome of these investigations. We are unable to determine when these matters will be resolved, whether any additional areas of inquiry will be opened, or any outcome of this matter. Any negative findings in this matter could result in fines, penalties, or program exclusions, which could have a material adverse effect on our financial condition, results of operations, and cash flows.

ITEM 4: SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of our security holders during the fourth quarter of the year ended December 31, 2007, through the solicitation of proxies or otherwise.

PART II

ITEM 5: MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is quoted on the NASDAQ Global Market under the symbol "NURO". The price range per share reflected in the table below is the high and low closing sales prices of our common stock as reported by NASDAQ for the periods indicated.

	Years ended December 31,			
	2007		2006	
	High	Low	High	Low
First quarter	$ 14.50	$ 9.25	$ 39.19	$ 28.00
Second quarter	$ 10.76	$ 8.62	$ 40.39	$ 25.73
Third quarter	$ 9.12	$ 7.25	$ 33.18	$ 18.74
Fourth quarter	$ 10.25	$ 7.79	$ 19.85	$ 13.52

On March 7, 2008, there were approximately 136 stockholders of record of our common stock. This number does not include stockholders for whom shares were held in a "nominee" or "street" name. On March 7, 2008, the last reported sale price per share of our common stock on the NASDAQ Global Market was $2.03.

We have never declared or paid any cash dividends on our common stock. We currently intend to retain future earnings, if any, to finance the expansion and growth of our business and do not expect to pay any cash dividends in the foreseeable future. Payment of future cash dividends, if any, will be at the discretion of our board of directors after taking into account various factors, including our financial condition, operating results, current and anticipated cash needs and plans for expansion.

See Part III, Item 12 for information regarding securities authorized for issuance under equity compensation plans.

COMPARATIVE STOCK PERFORMANCE GRAPH

The following graph shows the cumulative stockholder return of our common stock from July 22, 2004 (the first trading day for our common stock) through December 31, 2007 as compared with that of the Nasdaq (U.S. Companies) Index and the Nasdaq Medical Device Manufacturers Index. The total stockholder return is measured by dividing the per share price change of the respective securities, plus dividends, if any, for each period shown by the share price at the end of the particular period. The graph assumes the investment of $100 in our common stock and each of the comparison groups on July 22, 2004 and assumes the reinvestment of dividends. We have never declared a dividend on our common stock. The stock price performance depicted in the graph below is not necessarily indicative of future price performance.

	07/22/04	12/31/04	12/31/05	12/31/06	12/31/07
NeuroMetrix, Inc.	$ 100.00	$ 146.88	$ 341.00	$ 186.38	$ 115.00
Nasdaq Stock Market (U.S.)	$ 100.00	$ 115.25	$ 117.69	$ 129.32	$ 140.24
Nasdaq Medical Device Manuf. Index	$ 100.00	$ 112.49	$ 123.50	$ 130.24	$ 165.52

ITEM 6: SELECTED FINANCIAL DATA

The data set forth below should be read in conjunction with Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," Item 7A, "Quantitative and Qualitative Disclosures About Market Risk" and our financial statements and related notes appearing elsewhere in this Annual Report on Form 10-K.

	Years Ended December 31,				
	2007	2006	2005	2004	2003
	(In thousands, except share and per share data)				
Statement of Operations Data:					
Revenues	$ 44,622	$ 55,250	$ 34,298	$ 17,920	$ 9,168
Cost of revenues	12,062	13,558	8,858	4,853	2,707
Gross margin	32,560	41,692	25,440	13,067	6,461
Operating expenses:					
Research and development	4,892	5,011	3,821	3,268	2,397
Sales and marketing	22,964	22,014	14,150	8,488	4,768
General and administrative	14,834	11,805	8,022	5,267	3,052
Total operating expenses	42,690	38,829	25,993	17,024	10,217
Income (loss) from operations	(10,129)	2,862	(553)	(3,957)	(3,756)
Interest income (expense), net	1,751	1,598	837	(750)	(113)
Income (loss) before provision for income taxes	(8,378)	4,461	284	(4,707)	(3,869)
Provision for income taxes		193	35		
Net income (loss)	(8,378)	4,268	249	(4,707)	(3,869)
Accretion of dividend on redeemable convertible preferred stock				(1,386)	(2,009)
Deemed dividend on redeemable convertible preferred stock				(788)	
Beneficial conversion feature associated with redeemable convertible preferred stock				(7,051)	
Net income (loss) attributable to common stockholders	$ (8,378)	$ 4,268	$ 249	$ (13,932)	$ (5,878)
Net income (loss) per common share:					
Basic	$ (0.66)	$ 0.34	$ 0.02	$ (2.42)	$ (5.66)
Diluted	$ (0.66)	$ 0.33	$ 0.02	$ (2.42)	$ (5.66)
Weighted average common shares outstanding:					
Basic	12,628,310	12,501,742	12,152,139	5,747,579	1,038,817
Diluted	12,628,310	13,097,891	12,986,365	5,747,579	1,038,817

	As of December 31,				
	2007	2006	2005	2004	2003
	(in thousands)				
Balance Sheet Data:					
Cash and cash equivalents	$ 7,097	$ 7,910	$ 8,170	$ 1,936	$ 1,623
Short-term investments	22,622	32,411	24,082	18,575	
Working capital	33,304	41,894	33,268	21,774	2,451
Long-term investments	1,058			9,497	
Total assets	56,375	55,706	42,897	37,953	7,218
Long-term debt and other long-term liabilities	33	73	131	189	2,232
Warrants for redeemable convertible preferred stock					450
Redeemable convertible preferred stock					47,694
Accumulated deficit	(62,066)	(53,687)	(57,955)	(58,204)	(45,204)
Total stockholders' equity(deficit)	46,730	43,409	34,833	33,330	(45,805)

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion of our financial condition and results of operations in conjunction with our selected financial data, our condensed financial statements and the accompanying notes to those financial statements included elsewhere in this Annual Report on Form 10-K. This discussion contains forward-looking statements that involve risks and uncertainties. As a result of many factors, such as those set forth under the section titled "Risk Factors" and elsewhere in this Annual Report on Form 10-K, our actual results may differ materially from those anticipated in these forward-looking statements.

Overview

NeuroMetrix was founded in June 1996. We design, develop and market proprietary medical devices used to help physicians diagnose and treat diseases of the nervous system such as neuropathies, which are disorders of the peripheral nerves and parts of the spine, and neurovascular disorders such as diabetic retinopathy. We are also developing medical devices designed to be used to provide regional anesthesia and pain control. To date, our focus has been on products that help physicians with the diagnosis of neuropathies and neurovascular disorders. We have two products lines cleared by the United States Food and Drug Administration, or FDA, that are currently being marketed to physicians and clinics, including the NC-stat System for the assessment of neuropathies and the DigiScope for the detection of eye disorders such as diabetic retinopathy.

We believe that our neuropathy diagnostic system, the NC-stat System, improves the quality and efficiency of patient care by offering all physicians the ability to diagnose patients with neuropathies at the point-of-service, that is, in the physician's office at the time the patient is examined, resulting in earlier and more accurate detection, greater patient comfort and convenience, and, in many cases, improved clinical and economic outcomes. The NC-stat System is comprised of: (1) disposable single use NC-stat biosensors that are placed on the patient's body, (2) the NC-stat monitor and related components and (3) the NC-stat docking station, an optional device that enables the physician's office to transmit data to our onCall Information System. The NC-stat System has been on the market since May 1999 and is used in over 5,500 physician's offices and clinics in the United States. Over 1.0 million patients have had nerve conduction tests performed using the NC-stat System. Substantially all of our revenues to date have been derived from sales of the NC-stat System. We are currently developing a traditional nerve conduction system, the ADVANCE System, for the diagnosis of neuropathies and have filed a 510(k) application with the FDA. Presuming it is successfully commercialized, the ADVANCE System is expected to provide physicians with even greater clinical functionality and is expected to be marketed to specialists such as neurologists as well as primary care physicians.

Acquisition

On December 26, 2007, we acquired substantially all of the assets and assumed certain liabilities of EyeTel Imaging, Inc., or EyeTel, and their product, the DigiScope, a product used for the detection of eye disorders such as diabetic retinopathy, for 1,050,297 shares of common stock, $175,000 in cash and the assumption of certain liabilities.

Neurovascular disease includes conditions such as retinopathy, an eye disease prevalent in patients with diabetes. The DigiScope is marketed to the primary diabetes care physician office market and the optometry market. Prior to the acquisition of substantially all of the assets and the assumption of certain liabilities of EyeTel, we had been marketing the DigiScope to the primary diabetes care physician office market through an exclusive sales and marketing license with EyeTel. The DigiScope allows physicians to diagnose diabetic retinopathy and refer patients to an eye specialist for treatment if deemed necessary based on the results. It is recommended by the American Diabetes Association, or

ADA, that all patients with diabetes receive an annual dilated eye examination to monitor vision. According to the ADA, there are approximately 21.0 million people in the United States with diabetes and only approximately 50% comply with the recommendation to have an annual eye examination. We believe that a product such as the DigiScope in primary diabetes care physician offices and optometry clinics could potentially lead to an increase in the level of testing and result in the earlier detection of eye diseases in patients with diabetes and improved clinical outcomes.

Corporate Collaborations

In November 2007, we made an investment of $2.5 million for the purchase of approximately 5.4 million shares of common stock of Cyberkinetics Neurotechnology Systems, Inc., or Cyberkinetics, representing approximately 13% of the Cyberkinetics' issued and outstanding shares at the time of the investment, at a price of $0.46 per share. We also received a warrant to purchase up to approximately 2.7 million shares of Cyberkinetics common stock. The warrant, exercisable at $0.46 per share, has a term of five years, and is required to be exercised if Cyberkinetics receives FDA approval of a Humanitarian Device Exemption, or HDE, filing for the Andara Oscillating Field Stimulator , or Andara OFS, device for acute spinal cord injuries. In addition, we received a seat on the Cyberkinetics Board of Directors. Dr. Shai Gozani M.D. Ph.D., our Chief Executive Officer and President, has been named as our initial designee.

In connection with the investment in Cyberkinetics, we also received certain rights, including a right of first negotiation for the acquisition of Cyberkinetics and a right of first negotiation for the commercialization of the Andara OFS device for the treatment of acute spinal cord injuries.

In February 2008, we entered into a Collaboration Agreement and Operating Agreement with Cyberkinetics to develop and commercialize products for the treatment of peripheral nerve injury and formed PNIR (Peripheral Nerve Injury Repair) LLC, a joint venture with 50% ownership held by us and 50% ownership held by Cyberkinetics.

We derive the majority of our revenues from the sale of NC-stat biosensors, monitors and docking stations directly to end users, which are generally physician practice groups. Our NC-stat biosensors are disposable products that are used once and inactivated after use. The NC-stat monitor is an electronic instrument that is used with the NC-stat biosensors to perform nerve conduction studies for the purpose of diagnosing neuropathies. The NC-stat monitor displays the results of nerve conduction studies on a LCD screen immediately at the conclusion of each study. The NC-stat docking station is an optional device that is used to transmit to the onCall Information System data generated by the nerve conduction study performed with the NC-stat monitor. The onCall Information System automatically formulates the data it receives for each test into a detailed report that is provided to the customer through facsimile or e-mail.

We also derive revenues from sales of the DigiScope to physicians through (1) eye scan fees, (2) monthly rental fees and (3) installation and training fees. During 2007, we were required to remit a percentage of the revenues related to the DigiScope to EyeTel under our sales and marketing license with EyeTel. As a result of our acquisition of substantially all of the assets of EyeTel on December 26, 2007, we are no longer required to remit any revenues to EyeTel. In addition, we expanded the market opportunity for the DigiScope into the optometry market in addition to the primary diabetes care physician office market.

Our revenues declined to $44.6 million for the twelve months ended December 31, 2007, compared to $55.2 million for the same period in 2006. Additionally, we incurred a net loss of $8.4 million for the twelve months ended December 31, 2007, compared to net income of $4.3 million for the same period in 2006. We believe that the decline in our revenues has been caused primarily by adverse developments over the past year relating to the reimbursement by third-party payers of nerve conduction studies performed using the NC-stat System, and we expect that our revenues will continue

to be adversely affected by the uncertainty regarding reimbursement and by the outcome of the February 2008 AMA CPT Editorial Panel meeting to review the reimbursement coding for nerve conduction studies.

Significant developments impacting and relating to our financial condition and results of operations as of and for the year ended December 31, 2007 and expected to impact future periods include:

- the impact of reimbursement developments relating to nerve conduction studies on our revenues as described above, including the outcome of the AMA CPT Editorial Panel meeting and the material and adverse impact the potential issuance of a Category III CPT code by the AMA is likely to have on our revenues and operating results;

- expanded sales and marketing efforts for the DigiScope as a result of the acquisition of substantially all of the assets and the assumption of certain liabilities of EyeTel and the broader market opportunity we can now address including the optometry market. We expect to continue to increase revenues from the DigiScope and we expect that the gross margin on DigiScope revenues will improve due to our acquisition and the elimination of the amounts we were previously remitting to EyeTel;

- increased capital expenditures relating to purchases of DigiScope units, resulting from the acquisition of substantially all of the assets and the assumption of certain liabilities of EyeTel and our responsibility for all units produced by our third party manufacturer;

- our decision to terminate the relationships with our independent sales agencies in the second half of 2007, which we believe has adversely impacted our revenues, but is expected to reduce sales and marketing expenses in 2008 as a result of the elimination of commissions on recurring revenues from accounts originally sourced through our independent sales agencies. In 2007, total commissions relating to independent sales agencies were $3.0 million;

- the delay of the expected launch of the ADVANCE System, our traditional neurodiagnostic system, for which we have invested approximately $3.0 million in inventories as of December 31, 2007, and for which we continue to seek 510(k) regulatory approval from the FDA;

- the government investigations by the Office of Inspector General, or OIG, of the Department of Health and Human Services and the U.S. Department of Justice, or DOJ, that we are subject to, which resulted in significantly increased legal expenses in 2007. We cannot predict the potential impact of these investigations on our financial condition or financial results in 2008;

- continued progress with our product in development, referred to as NAVIGATOR, a minimally invasive nerve localization system for regional anesthesia, pain control and the treatment of neuropathies such as carpal tunnel syndrome, or CTS, for which we expect to file a 510(k) application with the FDA in 2008. We continue to invest resources on the development of this product; and

- the investment we made in Cyberkinetics in the fourth quarter of 2007, which included the purchase of $2.5 million of Cyberkinetics common stock and the receipt of a warrant to purchase an additional $1.25 million of Cyberkinetics common stock that we must exercise in certain circumstances, as well as the joint venture we have entered into with Cyberkinetics for the development of a treatment for peripheral nerve injury, for which we have committed to fund the first $2.0 million in development expenses and 50% of any development costs exceeding the initial $2.0 million.

Reimbursement from third-party payers is an important element of success for medical products companies. As our presence in the market expands and the use of the NC-stat System increases, we have experienced and are likely to continue to experience an increased focus from third-party payers and governmental agencies regarding the reimbursement of nerve conduction studies performed using

the NC-stat System and an increased focus from these organizations regarding the professional requirements for performing nerve conduction studies in general. A number of third-party payers, including commercial payers, have taken and may continue to take the position of not reimbursing our customers for their use of the NC-stat System.

During the second half of 2006 and in 2007, several local Medicare carriers issued draft LCDs, final LCDs or coding articles particularly addressing coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System. Several of these carriers indicated that they will not reimburse physicians under Medicare for nerve conduction studies performed using the NC-stat System under the three existing Current Procedural Terminology, or CPT, codes for conventional nerve conduction studies (95900, 95903 and 95904), which provide for levels of reimbursement fixed by the Center for Medicaid and Medicare Services, or CMS, but rather that physicians must submit claims for reimbursement for these procedures under a miscellaneous CPT code (95999), in which case the local carriers may determine the level of reimbursement to be paid, if any. Currently, there are three local Medicare carriers with final LCDs, one local Medicare carrier with a draft LCD, and one local Medicare carrier with a coding article which address coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System. One additional Medicare carrier, which had previously issued a final LCD, reversed their position effective June 30, 2007. In certain regions impacted by these reimbursement decisions, our customers have experienced lower levels of reimbursement and higher levels of claims denials. If physicians do not receive adequate reimbursement under the miscellaneous CPT code from those local carriers, our existing customers may continue to limit or curtail their use of the NC-stat System and we may be unable to obtain new customers, both of which could materially and adversely impact our revenues and profitability.

The AMA formed a work group in early 2007 to examine the reimbursement coding of nerve conduction studies and nerve conduction equipment, including the NC-stat System. The findings of this committee were presented to the AMA CPT Editorial Panel at a meeting in February 2008. During the CPT Panel meeting, several proposals for new Category I CPT codes, which generally are included in the Medicare physician fee schedule and are assigned specified reimbursement values, were presented by the chairpersons of the work group and were supported by several physician societies. In spite of this, the only proposal voted on was for the creation of a new Category III CPT code, which generally would not be included on the Medicare physician fee schedule and would not generally have an assigned reimbursement value. At this meeting, we believe that the CPT Panel approved a new Category III CPT Code for nerve conduction studies performed using equipment with certain automated features such as the NC-stat System. Unless we are able to successfully challenge this decision, a new Category III CPT Code would likely be published in July 2008 and become effective in January 2009. In the event that a Category III CPT code is published which describes nerve conduction studies performed with the NC-stat System, it would likely result in limited or no Medicare reimbursement for such studies as a result of the potential that no specified reimbursement values would be assigned to these codes. This could also adversely impact reimbursement by other third party payers and could have an adverse and material impact on our revenues and results of operations.

The LCDs and coding articles issued by local Medicare carriers have also addressed a number of other issues, including (1) the background and training of physicians supervising or performing nerve conduction studies, (2) the level of training requirements for technicians performing a nerve conduction study, (3) whether nerve conduction tests should be required to be performed concomitantly with a needle electromyography procedure and (4) whether the NC-stat System is comparable to conventional nerve conduction testing equipment. We do not believe that these LCDs prohibit physicians from receiving reimbursement under Medicare for medically necessary nerve conduction studies performed using the NC-stat System. However, these LCDs do appear to be targeted at limiting access to perform and/or reimbursement for nerve conduction studies. In certain cases, these LCDs are being interpreted

or implemented in a manner that impacts the ability of physicians to receive reimbursement under Medicare, including lower levels of reimbursement and an increase in the number of claims being denied, for nerve conduction studies performed using the NC-stat System, which are having an adverse impact on our revenues.

Additionally, a significant number of commercial payers, including the majority of regional Blue Cross Blue Shield carriers, and other major private payers, have adopted policies indicating that they will not provide reimbursement for the use of the NC-stat System. These commercial payers have cited various reasons for their reimbursement policies, including, among others, that the NC-stat System is experimental and investigational. We are in the process of communicating with these payers, directly, through our customers or through our network of reimbursement consultants, to attempt to address their concerns. Third-party payers may also impose requirements on physicians to submit additional paperwork supporting the medical necessity of nerve conduction studies performed using the NC-stat System. We believe these requirements are negatively impacting the use of the NC-stat System by existing customers and our sales to new customers, both of which are having an adverse impact on our revenues.

Additional third-party payers, including local Medicare carriers and commercial payers, could potentially take a position that could reduce or eliminate the reimbursement for the NC-stat System and could have the impact of deterring usage by our customers which could have an adverse impact on our revenues.

We believe that eye scans performed using the DigiScope are being reimbursed by the majority of third-party payers. Many commercial payers have policies in place providing for reimbursement for the use of the DigiScope and many of these payers have published favorable articles about the DigiScope in their newsletters. However, several Medicare carriers have issued draft LCDs and coding articles that require a diagnosis of pre-existing retinal disease and/or will only reimburse for fundus photography, a highly specialized form of medical imaging, when performed in conjunction with an eye examination performed by an eye specialist. There are no assurances that other Medicare carriers will not issue similar draft LCDs, final LCDs or coding articles restricting the reimbursement for the use of the DigiScope. We believe that eye examinations performed on patients covered by Medicare represented less than 25% of our DigiScope revenues in 2007. However, the restrictions on reimbursement by Medicare carriers could have an adverse impact on our ability to grow our DigiScope revenues in future periods.

One of the primary challenges we face in our business is successfully expanding the market for nerve conduction studies. A successful market expansion will depend upon, in part, our targeting of primary care and specialist physicians who traditionally have not been targeted by companies selling equipment used to perform nerve conduction studies and our ability to alter physicians' practices relating to the diagnosis of neuropathies. Our strategy had been to sell the NC-stat System through a combination of independent sales agencies and a direct sales force of experienced sales representatives. The independent sales agencies, including small to medium sized regional firms and larger national firms, had primarily been responsible for generating sales leads and our direct sales force had been responsible for bringing these sales leads to closure. These independent sales agencies typically had not served in a traditional distribution role and therefore had not been responsible for maintaining inventories, for making shipments to customers or for billing and collection functions.

Our strategy of utilizing independent sales agencies had been effective historically, but we experienced a significant decline in the percentage of new customers being sourced through our independent sales agency network in the first half of 2007. As a result, consistent with our long term business objectives, in the second half of 2007, we made a decision to terminate our relationships with all independent sales agencies and focus our selling efforts exclusively through our direct sales force,

which, as of December 31, 2007, was comprised of approximately 50 regional sales managers, five regional sales directors and one national sales director.

We expect that our direct sales force will expand their role in generating new customer sales leads, and we plan to increase efforts to generate sales leads through various marketing activities including mailings and tradeshows. However, we experienced a decline in the number of new customers added in the last several quarters along with a decline in sales to our existing customers. We believe the decision to terminate the independent sales agency relationships may have contributed to these declines and could potentially have an adverse impact on our revenues and our ability to secure new customers in future periods as well.

Business Focus

Our long-term financial objectives are to grow our business through the sale of proprietary medical devices and to achieve and sustain profitability. We expect to achieve these objectives through sales of the NC-stat System and the DigiScope and additional products that may be commercialized to help physicians in the diagnosis and treatment of nervous system disorders, including neuropathies, and neurovascular disorders and products designed to provide regional anesthesia and pain control. However, during 2008 our revenues are likely to continue to decline and we are likely to continue to incur losses as a result of the reimbursement and other issues we are currently facing. Our efforts in 2008 will focus on (1) efforts to manage the reimbursement challenges posed by third-party payers for the NC-stat System after the AMA CPT Editorial Panel issues their final determination on the reimbursement coding for nerve conduction studies performed using automated equipment such as the NC-stat System, (2) sales of the NC-stat System, (3) sales and marketing of the DigiScope for the detection of diabetic retinopathy, including a market expansion into optometry clinics, (4) seeking regulatory clearance from the FDA for our traditional neurodiagnostic system, the ADVANCE System, in order to launch this product into the specialist physician and primary care physician markets and for portions of the onCall Information System, (5) cooperating with, and working to resolve, the government investigations of which we are subject and (6) our ongoing research and development programs, including NAVIGATOR, and a peripheral nerve injury product being jointly developed with Cyberkinetics.

Our launch of the ADVANCE System will depend upon our receipt of regulatory clearance from the FDA. We submitted our initial 510(k) filing for the ADVANCE System in the first quarter of 2007 and FDA clearance is still pending. During the fourth quarter of 2006, at the request of the FDA, we submitted a 510(k) filing relating to portions of the onCall Information System that are currently in use and the 510(k) clearance is still pending. If 510(k) clearance for the portions of the onCall Information System that are under review is not obtained, it may require additional product development and potential changes in the configuration of our products.

With respect to our research and development programs, during 2008, we expect to continue efforts to develop new biosensors, on the development of the ADVANCE System and its accessories, on the development of NAVIGATOR, for which we anticipate filing a 510(k) application with the FDA in 2008, and on a product for the treatment of peripheral nerve injury in collaboration with our joint venture partner, Cyberkinetics.

Results of Operations

The following table presents certain statement of operations information stated as a percentage of total revenues:

	Years Ended December 31,		
	2007	2006	2005
Revenues:			
Diagnostic device	9.5%	13.6%	12.3%
Biosensor	88.3	86.4	87.7
Other	2.1		
Total revenues	100.0	100.0	100.0
Cost of revenues	27.0	24.5	25.8
Gross margin	73.0	75.5	74.2
Operating expenses:			
Research and development	11.0	9.1	11.1
Sales and marketing	51.5	39.8	41.3
General and administrative	33.2	21.4	23.4
Total operating expenses	95.7	70.3	75.8
Income (loss) from operations	(22.7)	5.2	(1.6)
Interest income, net	3.9	2.9	2.4
Income (loss) before provision for income taxes	(18.8)	8.1	0.8
Provision for income taxes		0.3	0.1
Net income (loss)	(18.8)%	7.7%	0.7%

Comparison of Years Ended December 31, 2007 and December 31, 2006

Revenues

The following tables present a breakdown of our customers, biosensor units used and revenues:

	Years Ended December 31,			
	2007	2006	Change	% Change
Customers	5,555	4,929	626	12.7%
Biosensor units used	1,055,500	1,155,300	(99,800)	(8.6)

	Years Ended December 31,			
	2007	2006	Change	% Change
	(in thousands, except percentage data)			
Revenues:				
Diagnostic device	$ 4,254.0	$ 7,538.3	$ (3,284.3)	(43.6)
Biosensor	39,413.3	47,711.4	(8,298.1)	(17.4)
Other	954.9		954.9	N/A
Total revenues	$ 44,622.2	$ 55,249.7	$ (10,627.5)	(19.2)

Diagnostic device revenues were $4.3 million and $7.5 million for the years ended December 31, 2007 and 2006, respectively, a decrease of $3.3 million, or 43.6%. This decrease is primarily attributable to a lower number of units sold, which we believe resulted primarily from uncertainty and adverse

developments relating to the reimbursement for procedures performed with the NC-stat System. Diagnostic device revenues accounted for 9.5% and 13.6% of our total revenues for the years ended December 31, 2007 and 2006, respectively.

Biosensor revenues were $39.4 million and $47.7 million for the years ended December 31, 2007 and 2006, respectively, a decrease of $8.3 million, or 17.4%. This decrease is attributable to lower sales of biosensors, which we believe resulted primarily from uncertainty and adverse developments relating to the reimbursement for procedures performed with the NC-stat System. Biosensor revenues accounted for 88.3% and 86.4% of our total revenues for the years ended December 31, 2007 and 2006, respectively.

Our customers used 1,055,500 biosensor units in the year ended December 31, 2007, compared to 1,155,300 units in the year ended December 31, 2006, a decrease of 99,800 units, or 8.6%. This decrease in biosensor usage is primarily the result of a decline in average usage per customer offset in part by an increase in our customer base. During the 12-month period ended December 31, 2007, a total of 5,555 customers used the NC-stat System compared to 4,929 customers for the same period in 2006. This represents a 12.7% year-over-year increase in the number of customers that used our NC-stat System. The average usage per account declined to 190 biosensors for the year ended December 31, 2007 from 234 biosensors for the same period in 2006.

Other revenues are attributable to the DigiScope, which we had been selling under an exclusive sales and marketing license agreement entered into with EyeTel in October 2006 and we launched our sales and marketing efforts during the first quarter of 2007. Revenues related to the DigiScope were derived from a mix of new customers and customer accounts that existed at the time of our signing of the license agreement with EyeTel and were transferred to us. On December 26, 2007, we acquired substantially all of the assets and assumed certain liabilities of EyeTel, including all the rights to the DigiScope.

Our total revenues were $44.6 million and $55.2 million for the years ended December 31, 2007 and 2006, respectively, a decrease of $10.6 million, or 19.2%. The decline in our total revenues is attributable to the previously mentioned lower number of NC-stat Systems and biosensors sold, which we believe resulted primarily from uncertainty and adverse developments relating to the reimbursement for nerve conduction studies performed with the NC-stat System.

We anticipate that revenues in 2008 will continue to decline. In the fourth quarter of 2007, we experienced a decline in revenues of 10.5% from the third quarter of 2007, which we believe primarily resulted from the uncertainty created by the issuance of draft LCDs, final LCDs and coding articles addressing reimbursement for nerve conduction studies and policies issued by commercial payers intended to deter usage or limit the reimbursement for the NC-stat System. These developments and other future reimbursement decisions, including the potential issuance of a Category III CPT code by the AMA CPT Editorial Panel, could continue to adversely impact reimbursement for procedures performed using the NC-stat System. Our revenues in 2008 are likely to be impacted by (a) the potential issuance of a Category III CPT code by the AMA CPT Editorial Panel; (b) the level of reimbursement, if any, established for procedures performed using the NC-stat System by insurance carriers and other third-party payers; (c) whether final LCDs are applied in a manner that places additional restrictions or qualifications on the performance of these procedures; (d) any other reimbursement determinations relating to nerve conduction studies that may be issued by third-party payers; or (e) any other events causing uncertainty as to the existence or amount of reimbursement physicians are likely to receive for performing procedures using the NC-stat System. Separately, we expect revenues to continue to be positively impacted by expanded sales and marketing efforts in the optometry market for the DigiScope. Overall, revenues could be impacted by a variety of factors, including the level of demand for our products, potential for changes in third-party reimbursement for nerve conduction studies, the decision to terminate our relationships with independent sales agencies,

the overall economy, competitive factors and the factors described in the section of this Annual Report on Form 10-K titled "Cautionary Note Regarding Forward-Looking Statements."

Costs and expenses

The following table presents our costs and expenses and net income (loss):

	Years Ended December 31,			
	2007	2006	Change	% Change
	(in thousands)			
Cost of revenues:				
Diagnostic device	$ 915.8	$ 1,320.5	$ (404.7)	(30.7)%
Biosensor	10,422.1	12,237.6	(1,815.5)	(14.8)
Other	724.0		724.0	N/A
Total cost of revenues	12,061.8	13,558.1	(1,496.3)	(11.0)
Gross margin:				
Diagnostic device	3,338.2	6,217.8	(2,879.6)	(46.3)
Biosensor	28,991.2	35,473.9	(6,482.6)	(18.3)
Other	231.0		231.0	N/A
Total gross margin	32,560.4	41,691.7	(9,131.2)	(21.9)
Gross Margin %:				
Diagnostic device	78.5%	82.5%		
Biosensor	73.6	74.4		
Other	24.2			
Total gross margin	73.0	75.5		
Operating expenses:				
Research and development	$ 4,891.9	$ 5,010.5	$ (118.6)	(2.4)
Sales and marketing	22,963.8	22,013.7	950.2	4.3
General and administrative	14,834.1	11,805.1	3,029.0	25.7
Total operating expenses	42,689.9	38,829.3	3,860.6	9.9
Income (loss) from operations	(10,129.4)	2,862.4	(12,991.8)	(453.9)
Interest income	1,751.0	1,598.4	152.6	9.5
Income (loss) before provision for income taxes	(8,378.5)	4,460.8	(12,839.3)	(287.8)
Provision for income taxes		193.0	(193.0)	(100.0)
Net income (loss) available to common stockholders	$ (8,378.5)	$ 4,267.8	$ (12,646.3)	(296.3)

Gross Margin

Diagnostic device gross margin decreased to $3.3 million, or 78.5% of diagnostic device revenue, for the year ended December 31, 2007, as compared to $6.2 million, or 82.5% of diagnostic device revenue, for same period in 2006. The decrease in the gross margin percentage is primarily attributable to a decrease in the number of devices sold.

Biosensor gross margin decreased to $29.0 million, or 73.6% of biosensor revenue, for the year ended December 31, 2007, as compared to $35.5 million, or 74.4% of biosensor revenue, for the same period in 2006. The decrease in the biosensor gross margin percentage is primarily due to lower sales volumes and higher product warranty costs.

Other gross margin percentage, which related entirely to the DigiScope, was 24.2% for the year ended December 31, 2007. DigiScope revenues in 2007 represent monthly rental fees and eye scan fees as well as the amortization of deferred revenues relating to installation and training fees. Under the

terms of agreement, we were required to remit a percentage of the revenues related to the DigiScope to EyeTel. The agreement included a provision for a higher percentage of the scan fees to be remitted to EyeTel for these existing customers for the first nine months of 2007. Effective October 1, 2007, consistent with the terms of our original agreement with EyeTel, the percentage of revenues we retained from these existing customers increased from 25% to 50%, which resulted in an increase in gross margins on DigiScope revenues in the fourth quarter of 2007 to 30.7% from 25.0% in the third quarter of 2007. As a result of our December 26, 2007 acquisition of substantially all of the assets of EyeTel, we expect gross margin on DigiScope revenues will increase in 2008.

Our overall gross margin decreased to $32.6 million, or 73.0% of revenues, for the year ended December 31, 2007, as compared to $41.7 million, or 75.5% of revenues, for same period in 2006.

Our gross margins may continue to decline during 2008 due to the expected decline in revenues derived from the NC-stat System and due to an expected increase in the percentage of total revenues derived from the DigiScope, which has lower gross margins as compared with our other products.

Research and Development

Our research and development, or R&D, expenses include expenses associated with our research, product development, clinical, regulatory, and quality assurance departments.

R&D expenses decreased $118,600, or 2.4%, to $4.9 million for the year ended December 31, 2007 from $5.0 million for the year ended December 31, 2006. As a percentage of revenues, R&D expenses were 11.0% and 9.1% for the years ended December 31, 2007 and 2006, respectively. The decrease in R&D expenses for the year ended December 31, 2007 compared with the same period in 2006, was primarily due to a decrease of $178,400 related to developmental costs expended on the ADVANCE System and on new biosensors. This decrease was offset in part by an increase of $81,000 in personnel costs resulting from the hiring of additional employees in our R&D department and related to increases in employee compensation.

We expect our spending on R&D will be relatively unchanged during 2008. We anticipate that resources devoted to the development of the ADVANCE System may be reallocated to other research and development efforts. This amount may vary, however, depending on the opportunities and challenges that arise during the year and depending on the outcome of the FDA review of our 510(k) submission for the ADVANCE System, the FDA review of our 510(K) submission for portions of the onCall Information System and our revenues during 2008.

Sales and Marketing

Our sales and marketing expenses include expenses from the marketing, field sales, sales administration and reimbursement departments.

Sales and marketing expenses increased $950,200, or 4.3%, to $23.0 million for year ended December 31, 2007 from $22.0 million for the year ended December 31, 2006. As a percentage of revenues, sales and marketing expenses were 51.5% and 39.8% for the years ended December 31, 2007 and 2006, respectively. The increase in expenses was primarily due to (a) an increase of $1.4 million in employee compensation and benefit costs attributable to the expansion of our sales force; (b) an increase of $511,100 in consulting services, primarily to assist us with the reimbursement challenges we are facing; (c) an increase of $245,400 in stock-based compensation expense; and (d) an increase of $335,400 in advertising and promotional expenses. These amounts were partially offset by a decrease in third-party sales commissions of $2.0 million, primarily due to our decision to terminate our relationships with all independent sales agencies and focus our selling efforts exclusively through our direct sales force and also due to decreased revenues.

We anticipate that our sales and marketing expenses may decline in 2008 as a result of reduced payments to independent sales agencies and reduced commissions to our direct sales force attributable to potentially lower revenues, however, this may vary, depending primarily upon on our revenues for 2008.

Our sales force is comprised of 56 employees, including 50 regional sales managers, as of December 31, 2007 compared to 53 employees, including 50 regional sales managers as of December 31, 2006. We plan to continue selling the DigiScope through the same sales force used to sell the NC-stat System and as a result we do not anticipate the need to expand the sales force to support the sales and marketing efforts for the DigiScope.

General and Administrative

Our general and administrative expenses include expenses from the executive, finance, administrative, customer service, and information technology departments.

General and administrative expenses increased $3.0 million, or 25.7%, to $14.8 million for year ended December 31, 2007 from $11.8 million for the year ended December 31, 2006. As a percentage of revenues, general and administrative expenses were 33.2% and 21.4% for the years ended December 31, 2007 and 2006, respectively. The increase in expenses was primarily due to an increase of $5.2 million in professional fees, mainly legal services, an increase of $425,000 in consulting expenses and an increase of $191,800 in stock-based compensation expense. The increases in professional fees and consulting services are both primarily related to the government investigations previously disclosed by us and to reimbursement matters. Partially offsetting these increases was a reversal of $1.7 million of sales tax liability as a result of receiving amnesty from a number of states and receiving relief from other states in the form of a limited look back period and waiver of penalties and a $585,200 decrease in bad debt expense.

We believe our general and administrative expenses will increase in 2008 as a result of our acquisition of substantially all of the assets of EyeTel and may increase or decrease depending upon the amount incurred for professional fees and consulting services relating to the government investigations and reimbursement matters previously disclosed by us.

Interest Income

Interest income was $1.8 million and $1.6 million during the years ended December 31, 2007 and 2006, respectively. Interest income was earned from cash equivalents and short-term investments. The increase in interest income for the year ended December 31, 2007, as compared to the same period in 2006, was primarily due to higher average invested cash balances combined with an increase in the average portfolio yield, attributable to a shift in the portfolio mix to higher yielding fixed maturities, and the prevailing interest rate environment primarily during the first half of 2007.

Provision for Income Taxes

We recorded no tax provision for the year ended December 31, 2007 due to the net loss incurred. We recorded a tax provision related to the alternative minimum tax of $193,000 for the year ended December 31, 2006.

Comparison of Years Ended December 31, 2006 and December 31, 2005

Revenues

The following tables present a breakdown of our customers, biosensor units used and revenues:

	Years Ended December 31,			
	2006	2005	Change	% Change
Customers	4,929	3,282	1,647	50.2%
Biosensor units used	1,155,300	704,800	450,500	63.9

	Years Ended December 31,			
	2006	2005	Change	% Change
	(in thousands, except percentage data)			
Revenues:				
Diagnostic device	$ 7,538.3	$ 4,221.3	$ 3,317.0	78.6
Biosensor	47,711.4	30,076.8	17,634.6	58.6
Total revenues	$ 55,249.7	$ 34,298.1	$ 20,951.6	61.1

Diagnostic device revenues were $7.5 million and $4.2 million for the years ended December 31, 2006 and 2005, respectively, an increase of $3.3 million, or 78.6%. Of this increase, approximately $2.6 million is attributable to a greater number of units sold, primarily as a result of increased demand for the NC-stat System and an increase in the number of regional sales managers. In addition, $0.7 million of this increase is attributable to an increase in the list price of our NC-stat monitors and docking stations from $4,000 to $5,000 effective January 1, 2006, which resulted in a higher average selling price during 2006 as compared to 2005. Diagnostic device revenues accounted for 13.6% and 12.3% of our total revenues for the years ended December 31, 2006 and 2005, respectively.

Biosensor revenues were $47.7 million and $30.1 million for the years ended December 31, 2006 and 2005, respectively, an increase of $17.6 million, or 58.6%. The increase is primarily due to an increased customer base for our biosensors and an increased frequency of testing by our customers. Biosensor revenues accounted for 86.4% and 87.7% of our total revenues for the years ended December 31, 2006 and 2005, respectively.

Our customers used 1,155,300 biosensor units in the year ended December 31, 2006, compared to 704,800 units in the year ended December 31, 2005, an increase of 450,500 units, or 63.9%. The increase in biosensor usage is primarily attributable to the increase in our customer base and to an increase in usage per customer. During the 12-month period ending December 31, 2006, a total of 4,929 customers used our NC-stat System compared to 3,282 customers for the same period ending December 31, 2005. This represents a 50.2% year-over-year increase in the number of customers that used our NC-stat System. The average usage per account increased to 234 biosensors for the year ended December 31, 2006 from 215 biosensors for the same period in 2005.

Our total revenues were $55.2 million and $34.3 million for the years ended December 31, 2006 and 2005, respectively, an increase of $21.0 million, or 61.1%.

Costs and expenses

The following table presents our costs and expenses and net income:

	Years Ended December 31,			
	2006	2005	Change	% Change
	(in thousands)			
Cost of revenues:				
Diagnostic device	$ 1,320.5	$ 1,059.7	$ 260.8	24.6%
Biosensor	12,237.6	7,798.4	4,439.2 4	56.9
Total cost of revenues	13,558.1	8,858.1	4,700.0	53.1
Gross margin:				
Diagnostic device	6,217.8	3,161.6	3,056.2	96.7
Biosensor	35,473.9	22,278.5	13,195.4	59.2
Total gross margin	41,691.7	25,440.0	16,251.6	63.9
Gross Margin %:				
Diagnostic device	82.5%	74.9%		
Biosensor	74.4	74.1		
Total gross margin	75.5	74.2		
Operating expenses:				
Research and development	$ 5,010.5	$ 3,820.6	$ 1,189.9	31.1
Sales and marketing	22,013.7	14,150.2	7,863.5	55.6
General and administrative	11,805.1	8,021.8	3,783.3	47.2
Total operating expenses	38,829.3	25,992.6	12,836.7	49.4
Income from operations	2,862.4	(552.5)	3,414.9	(618.1)
Interest income	1,598.4	838.8	759.6	90.6
Interest expense		(2.0)	2.0	(100.0)
Income before provision for income taxes	4,460.8	284.3	4,176.5	1,469.3
Provision for income taxes	193.0	35.0	158.0	451.4
Net income available to common stockholders	$ 4,267.8	$ 249.3	$ 4,018.5	1,612.2

Gross Margin

Diagnostic device gross margin increased to $6.2 million, or 82.5% of diagnostic device revenue, for the year ended December 31, 2006, as compared to $3.2 million, or 74.9% of diagnostic device revenue, for same period in 2005. The increase in the gross margin percentage in 2006 compared to 2005 is primarily attributable to an increase in the list price of our NC-stat System from $4,000 to $5,000 effective January 1, 2006 and manufacturing price reductions realized for our device beginning in the second quarter of 2006.

Biosensor gross margin increased to $35.5 million, or 74.4% of biosensor revenue for the year ended December 31, 2006, as compared to $22.3 million, or 74.1% of biosensor revenue, for the same period in 2005. The increase in biosensor gross margin percentage is primarily due to manufacturing price reductions realized for several of our biosensors during the second half of 2005 and the first quarter of 2006 partially offset by a change in the mix of biosensors sold.

Our overall gross margin increased to $41.7 million, or 75.5% of revenues, for the year ended December 31, 2006, as compared to $25.4 million, or 74.2% of revenues, for same period in 2005.

Research and Development

R&D expenses increased $1.2 million, or 31.1%, to $5.0 million for the year ended December 31, 2006 from $3.8 million for the year ended December 31, 2005. As a percentage of revenues, R&D expenses were 9.1% and 11.1% for the years ended December 31, 2006 and 2005, respectively. The increase in expenses is primarily due to an increase of $614,000 in personnel costs resulting from the hiring of additional employees in our R&D department and increases in employee compensation. In addition, product development and temporary labor costs increased $77,700 and $51,700, respectively. These increases are primarily related to the development of the ADVANCE System and new biosensors. Also contributing to the increase was an increase of $393,200 in stock-based compensation expense due to the adoption of the provisions of Statement of Financial Accounting Standards, or SFAS, No. 123(R), "*Share Based Payment*," or SFAS No. 123(R).

Sales and Marketing

Sales and marketing expenses increased $7.9 million, or 55.6%, to $22.0 million for year ended December 31, 2006 from $14.2 million for the year ended December 31, 2005. As a percentage of revenues, sales and marketing expenses were 39.8% and 41.3% for the years ended December 31, 2006 and 2005, respectively. The change in expenses is primarily due to an increase of $4.1 million in employee compensation and benefit costs, including sales commissions paid to our regional sales managers. This increase is attributable to the expansion of the sales force and higher revenues in 2006 as compared to 2005. Also contributing to the change in expenses are (a) an increase of $1.6 million in sales commissions paid to our independent regional sales agencies, which is related to our higher revenues in 2006 as well as the addition of a distributor in May 2006; (b) an increase in stock-based compensation expense of $653,300 due to the adoption of the provisions of SFAS No. 123(R); (c) an increase of $400,700 in travel expenses due to the expansion of the sales force; (d) an increase in consulting services of $299,300, primarily to assist us with reimbursement matters; and (e) an increase of $267,500 in costs for new promotional materials.

General and Administrative

General and administrative expenses increased $3.8 million, or 47.2%, to $11.8 million for year ended December 31, 2006 from $8.0 million for the year ended December 31, 2005. As a percentage of revenues, general and administrative expenses were 21.4% and 23.4% for the years ended December 31, 2006 and 2005, respectively. The increase in expenses is primarily due to (a) an increase in stock-based compensation expense of $1.2 million from the adoption of the provisions of SFAS No. 123(R); (b) an increase of $661,300 in bad debt expense resulting from an increase in past due accounts; (c) an increase of $538,400 in professional fees for legal services; (d) an increase of $456,000 in our accrual for sales taxes; (e) an increase of $268,800 in our insurance costs; (f) an increase in credit card and bank fees of $238,800 related to increased customer transactions; and (g) an increase in personnel costs of $120,700 from the expansion of staff and increases in employee compensation.

Interest Income

Interest income was $1,598,400 and $838,800 during the years ended December 31, 2006 and 2005, respectively, representing an increase of $759,600. Interest income was earned from cash equivalents, short-term investments and long-term investments. The increase in interest income for the year ended December 31, 2006, as compared to the year ended December 31, 2005 is primarily due to higher average cash balances and an increase in the average portfolio yield attributable to the impact of higher market interest rates in 2006. Interest expense was not material for the years ended December 31, 2006 and 2005.

Provision for Income Taxes

We recorded a tax provision related to alternative minimum tax of $193,000 and $35,000 for the years ended December 31, 2006 and 2005, respectively.

Liquidity and Capital Resources

Our principal source of liquidity is our current cash and cash equivalents and short-term held-to-maturity investments. As of December 31, 2007, the weighted average maturity of our short-term held-to-maturity investments was 136 days. Our ability to generate cash from operations is dependent upon our ability to generate revenue from sales of our products, as well as our ability to manage our operating costs and net assets. A decrease in demand for our products or unanticipated increases in our operating costs would likely have an adverse effect on our liquidity and cash generated from operations. The following sets forth information relating to our liquidity:

	December 31,			
	2007	2006	Change	% Change
	(in thousands)			
Cash and cash equivalents	$ 7,097.2	$ 7,909.8	$ (812.6)	(10.3)%
Short-term held-to-maturity investments	22,621.7	32,410.7	(9,788.9)	(30.2)
Total cash, cash equivalents and short-term held-to-maturity investments	$ 29,718.9	$ 40,320.5	$ (10,601.5)	(26.3)%

During 2007, our cash and cash equivalents and short-term held-to-maturity investments decreased by $10.6 million, primarily due to $8.0 million of cash used in operations, $2.5 million of cash used for our investment in Cyberkinetics common stock, $257,500 of cash used for capital expenditures and $175,000 of cash used to fund our acquisition of substantially all of the assets of EyeTel, offset partially by $285,900 of proceeds received from the issuance of common stock under our employee stock purchase plan and the exercise of stock options. The current estimated market value of the $2.5 million investment made in Cyberkinetics common stock is approximately $1.4 million and we are restricted from selling this investment until November 2008.

In managing our working capital, two of the financial measurements we monitor are days' sales outstanding, or DSO, and inventory turnover rate, which are presented in the table below for the years ended December 31, 2007 and 2006:

	Years Ended December 31,	
	2007	2006
Days' sales outstanding (days)	54	40
Inventory turnover rate (times per year)	2.7	4.3

Our payment terms extended to our customers generally require payment within 30 days from invoice date. At December 31, 2007, we experienced an increase in DSO to 54 days from 40 days at December 31, 2006 attributable to a significant increase in the percentage of accounts receivable past due 60 days that began during the fourth quarter of 2006. We believe that these increases were primarily the result of challenges surrounding the reimbursement by Medicare and commercial payers in certain regions of the United States for nerve conduction studies performed using the NC-stat System. As long as we continue to face these reimbursement challenges our DSO and our working capital may continue to be adversely impacted. Accounts payable are normally paid within 30 to 40 days from receipt of a vendor's invoice.

Our inventory turnover for the year ended December 31, 2007 was 2.7 times, compared with 4.3 times for the year ended December 31, 2006. The decrease in the inventory turnover rate for the year ended December 31, 2007, as compared to the year ended December 31, 2006, was primarily due to the initial production of the ADVANCE System and decreased demand for the NC-stat System, offset in part by a decline in inventories of biosensors due to production challenges being experienced by our third-party manufacturer resulting from their transition to a new manufacturing facility.

The following sets forth information relating to the sources and uses of our cash.

	Years Ended December 31,		
	2007	2006	2005
	(in thousands)		
Net cash provided by (used in) operating activities	$ (7,989.1)	$ 7,297.9	$ 1,908.1
Net cash provided by (used in) investing activities	$ 6,898.2	$ (9,133.4)	$ 3,514.5
Net cash provided by financing activities	$ 278.3	$ 1,575.3	$ 812.2

Our operating activities used $8.0 million of cash in 2007 while providing cash of $7.3 million and $1.9 million in 2006 and 2005, respectively. In 2007, a net loss of $8.4 million and a net use of cash of $3.4 million for our investment in working capital were offset by $3.8 million in non-cash items, mainly compensation expense associated with stock options. The primary driver for the use of cash in our investment in working capital was a decrease in accrued expenses of $3.4 million. This decrease was primarily due to the reversal of $1.7 million of sales tax liability as a result of receiving amnesty from a number of states and receiving relief from other states in the form of a limited look back period and waiver of penalties. Also impacting working capital was an increase in our inventories of $1.7 million primarily for the production of the ADVANCE System. These items were offset by a $1.6 million decrease in accounts receivable, excluding the provision for doubtful accounts, due to a decline in revenues. In 2006, a net use of cash of approximately $1.2 million for our investment in working capital was offset by $4.3 million in net income and $4.2 million in non-cash items, mainly compensation expense associated with stock options. The primary drivers of our investment in working capital were as follows: our accounts receivable increased $4.1 million, excluding the change in the allowance for doubtful accounts, primarily due to growth in revenues and our inventories increased $950,000 primarily due to the growth in our business and our preparation for the release of the ADVANCE System. These items were partially offset by a $2.1 million increase in accrued expenses. In 2005, increases in accrued expenses, deferred revenue (net of deferred costs) and accounts payable of $1.9 million, $588,900 and $799,300, respectively; non-cash items of $1.4 million and net income of $249,300 were offset in part by increases in accounts receivable and inventory of $1.7 million and $1.4 million, respectively.

As a result of the decline in revenues and increase in operating expenses, we incurred a net loss in 2007 and we expect to incur increased net losses for 2008. This is expected to have an adverse impact on our cash flows from operating activities for 2008.

Our investing activities provided $6.9 million of cash in 2007, used $9.1 million of cash in 2006 and provided $3.5 million of cash in 2005. In 2007, $37.8 million in investment maturities provided cash which was offset in part by $28.0 million in investment purchases, $2.5 million used to fund our investment in Cyberkinetics, $257,500 used to fund purchases of fixed assets, primarily related to computer equipment and tooling equipment for new products and $175,000 used to fund the acquisition of substantially all of the assets of EyeTel. In 2006, $42.1 million in investment purchases and $620,500 used to fund purchases of fixed assets, primarily related to computer equipment, were partially offset by $33.6 million in cash provided from investment maturities. In 2005, $18.8 million in investment maturities provided cash which was offset by $15.3 million in investment purchases, which was primarily reinvested in cash equivalents and $475,100 used to fund purchases of fixed assets primarily related to leasehold improvements and tooling equipment for new products.

During 2008, we expect to continue to maintain our cash and investments in money market funds and short-term investment vehicles. We currently have a commitment of approximately $487,600 to purchase DigiScopes from our manufacturer in China. We expect that our capital expenditures will increase in 2008 compared with 2007 due to the purchases of DigiScopes. We anticipate a total capital investment for DigiScopes in 2008 of $1.6 million to $2.0 million, including the commitment referred to above. Additionally we have a potential commitment to purchase an additional $1.25 million of Cyberkinetics common stock that we must exercise in certain circumstances.

In February 2008, our property lease, originally entered into at the beginning of January 2001 and which was scheduled to expire on March 31, 2009, was amended to extend the term of the lease for a period of an additional four years. In connection with this amendment, the amount of the irrevocable standby letter of credit, we are required to maintain, stating the lessor as the beneficiary, will be reduced from $1,430,000 to $400,000. The letter of credit must be secured by a certificate of deposit in an amount equal to 102% of the letter of credit as a security deposit. We expect that this reduction in the security deposit of approximately $1.0 million will become available to us for our operating and working capital needs during the first half of 2008. The lease will now expire in March 2013. The certificate of deposit is renewable annually. This amount is classified as restricted cash in the balance sheet.

Our financing activities provided $278,300, $1.6 million and $812,000 of cash in 2007, 2006 and 2005, respectively. Cash provided by financing activities in 2007, 2006 and 2005 represent the proceeds from the issuance of shares under our employee stock purchase plan and the exercise of stock options. In 2007, these proceeds were offset in part by payments on a capital lease.

During 2008, we plan to fund sales and marketing efforts for the DigiScope and continue our research and development programs, including the ADVANCE System. We plan to continue investing resources on the development of NAVIGATOR, a minimally invasive nerve localization system for regional anesthesia, pain control and the treatment of neuropathies such as CTS. We also expect to incur capital expenditures for computer hardware and software to support our business and the additional requirements of our customer base. We also continue to explore investment, licensing and acquisition opportunities that may expand our product offering in the physician office market and in the neurological sector.

We expect to continue to incur net losses and negative cash flows from operations for the foreseeable future. Based upon our current plans, we believe that our existing capital resources, including cash and cash equivalents and short-term investments, as of December 31, 2007 are sufficient to finance our ongoing operations for twenty-four months, including the anticipated operating expenses and capital expenditures described above. However, our business is currently facing significant challenges and uncertainties and, as a result, our available capital resources may be consumed more rapidly than currently expected due to changes in our estimates, future revenues, changes we make to our ongoing operating expenses, future changes in our business strategy, decisions we make regarding the size of our sales force and the magnitude of our sales and marketing programs, research and development spending plans, the outcome of the DOJ investigation that we are currently subject to, and other items affecting our level of expenditures and our use of existing cash and cash equivalents and short-term investments. Accordingly, we may need to raise additional funds to support our operating and capital needs. Without additional funds, we may be forced to delay, scale back or eliminate some of our sales and marketing efforts, research and development activities or other operations and potentially delay our product development efforts.

We may attempt to obtain additional funding through public or private financing, collaborative arrangements with strategic partners or through additional credit lines or other debt financing sources to increase the funds we have available to us to fund our operations. However, there are no assurances that we will be able to secure such financing on favorable terms, if at all.

As of December 31, 2007, we have federal and state net operating loss carryforwards available to offset future taxable income of $37.0 million and $21.1 million, respectively, and federal and state research and development credits of $598,000 and $544,000, respectively, which may be available to reduce future taxable income and the related taxes thereon. The net operating loss and research and development credit carryforwards expire at various dates beginning in 2011 for federal and 2008 for state. Ownership changes in our company, as defined in the Internal Revenue Code, are expected to have a modest limitation on the amount of net operating loss and research and development credit carryforwards that can be utilized annually to offset future taxable income and taxes, based on an analysis of the provisions of Section 382 of the Internal Revenue Code. Subsequent changes in our ownership could further affect the limitation in future years.

To date, inflation has not had a material impact on our financial operations.

Off-Balance Sheet Arrangements, Contractual Obligations and Contingent Liabilities and Commitments

As of December 31, 2007, we did not have any off-balance sheet financing arrangements.

The following table summarizes our principal contractual obligations as of December 31, 2007 and the effects such obligations are expected to have on our liquidity and cash flows in future periods.

	Payments due in					
Contractual Obligations	**Total**	**2008**	**2009**	**2010**	**2011 & 2012**	**after 2012**
Operating lease obligations	$ 1,162,500	$ 930,000	$ 232,500	$	$	$
Capital lease obligations	31,175	12,900	12,900	5,375		
Purchase order obligations	3,369,946	3,369,946				
Total contractual obligations	$ 4,563,621	$ 4,312,846	$ 245,400	$ 5,375	$	$

In connection with our investment in Cyberkinetics, we received a warrant to purchase up to approximately 2.7 million shares of Cyberkinetics common stock. The warrant, exercisable at $0.46 per share, or approximately $1.25 million, has a term of five years, and is required to be exercised by us if Cyberkinetics receives FDA approval of an HDE filing for the Andara OFS device for acute spinal cord injuries.

In February 2008, we entered into a Collaboration Agreement and Operating Agreement with Cyberkinetics to develop and commercialize products for the treatment of peripheral nerve injury and formed PNIR (Peripheral Nerve Injury Repair) LLC, a joint venture with initial ownership of 50% held by us and 50% held by Cyberkinetics. Under the terms of the joint venture, we have agreed to fund the initial $2.0 million in product development costs and have agreed to share equally in all costs in excess of the initial $2.0 million.

In February 2008, we amended the Lease Agreement dated October 18, 2000 between Fourth Avenue LLC and us for office and engineering laboratory space. The amendment extends the term of the lease, currently scheduled to expire on March 31, 2009, through March 31, 2013. Base rent for the period April 2009 through March 2013 will be reduced from the current level of $930,000 annually to a range of $675,000 to $765,000 annually.

Critical Accounting Policies

Our financial statements are based on the selection and application of generally accepted accounting principles, which require us to make estimates and assumptions about future events that affect the amounts reported in our financial statements and the accompanying notes. Future events and their effects cannot be determined with certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results could differ from those estimates, and any such differences may

be material to our financial statements. We believe that the policies set forth below may involve a higher degree of judgment and complexity in their application than our other accounting policies and represent the critical accounting policies used in the preparation of our financial statements. If different assumptions or conditions were to prevail, the results could be materially different from our reported results. Our significant accounting policies are presented within Note 1 to our Financial Statements.

Revenue Recognition

Our revenue recognition policy is to recognize revenues from our NC-stat System monitors and biosensors upon shipment if the fee is fixed or determinable, persuasive evidence of an arrangement exists, delivery has occurred and risk of loss has passed, collection of the resulting receivables is reasonably assured and product returns are reasonably estimable. Revenues from our docking station and access to the onCall Information System are considered one unit of accounting and are deferred and recognized over the shorter of the estimated customer relationship period or the estimated useful life of the product, currently three years. We record revenue on a net basis for product sales made to distributors, based upon the amount billed to the distributors, when the distributor accepts the responsibility for invoicing the customer and the responsibility for the risk of collections and product returns from the customer.

When multiple elements are contained in a single arrangement, we allocate revenue between the elements based on their relative fair value, provided that each element meets the criteria for treatment as a separate unit of accounting. An element is considered a separate unit of accounting if it has value to the customer on a stand-alone basis, there is objective, reliable evidence of the fair value of the undelivered elements and delivery or performance of the undelivered elements is considered probable and substantially in our control. Fair value is determined based upon the price charged when the element is sold separately.

Revenue recognition involves judgments, including assessments of expected returns, allowance for doubtful accounts and expected customer relationship periods. We analyze various factors, including a review of specific transactions, our historical returns, average customer relationship periods, customer usage, customer balances and market and economic conditions. Changes in judgments or estimates on these factors could materially impact the timing and amount of revenues and costs recognized. Should market or economic conditions deteriorate, our actual return or bad debt experience could exceed our estimate.

Certain product sales are made with a 30-day right of return. Since we can reasonably estimate future returns, we recognize revenues associated with product sales that contain a right of return upon shipment and at the same time reduce revenue by the amount of estimated returns under the provisions of SFAS No. 48, "*Revenue Recognition When Right of Return Exists*."

Other revenues consist entirely of revenues relating to the DigiScope, including installation and training fees, per patient fees for eye scans performed using the DigiScope and monthly rental fees for the use of the DigiScope. Installation and training fees are deferred and recognized on a straight line basis over the non-cancelable term of the customer contract, currently one year. Revenues from fees charged for patient eye scans are recognized as the scans are performed. Fees for the rental of the DigiScope are recognized on a monthly basis. Under the terms of an exclusive sales and marketing license to the DigiScope from EyeTel, amounts due to EyeTel were recorded as cost of sales.

Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in our existing accounts receivable. We review our allowance for doubtful accounts and determine the allowance based on an analysis of customer past payment history, product usage activity, and recent

communications between us and the customer. Past due balances over 90 days are reviewed individually for collectibility. Account balances are charged off against the allowance when we feel it is probable the receivable will not be recovered. We do not have any off-balance sheet credit exposure related to our customers.

Warranty Costs

We accrue for device and biosensor warranty costs at the time of sale. While we engage in extensive product quality programs and processes, our warranty obligation is affected by product failure rates, user error, variability in physiology and anatomy of customers' patients, material usage and delivery costs. Should actual product failure and user error rates, material usage or delivery costs differ from our estimates, the amount of actual warranty costs could materially differ from our estimates. Warranty costs are based on the cost of repairing or replacing monitors and docking stations and based on the replacement cost of biosensors.

Asset Valuation

Asset valuation includes assessing the recorded value of certain assets, including short and long-term investments, accounts receivable, inventories and fixed assets. We use a variety of factors to assess valuation, depending upon the asset. Our investment portfolio is classified as held-to-maturity, and such investments are stated at amortized cost. In accordance with the provisions of SFAS No. 115, "*Accounting for Certain Investments in Debt and Equity Securities*", or SFAS No. 115, our investment in Cyberkinetics is classified as available-for-sale and is carried at fair value, with any unrealized gains and losses, net of taxes, reported in accumulated other comprehensive loss, a separate component of stockholders' equity. Accounts receivable are evaluated based upon our historical experience, the age of the receivable and current market and economic conditions. The realizable value of inventories is based upon the types and levels of inventory held, forecasted demand, pricing, competition and changes in technology. Should current market and economic conditions deteriorate, our actual recoveries could be less than our estimates. The recoverability of our fixed assets and other long-lived assets are evaluated when circumstances indicate that an event of impairment may have occurred in accordance with the provisions of SFAS No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets*", or SFAS No. 144.

Accounting for Income Taxes

As part of the process of preparing our financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure, including assessing the risks associated with tax audits, together with assessing temporary differences resulting from the different treatment of items for tax and accounting purposes. These differences, together with cumulative net operating losses, result in deferred tax assets and liabilities, which are included within our balance sheet. We assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not more likely than not, establish a valuation allowance. The primary factor used in the determination of the valuation allowance is our historical profitability. In the event that actual results differ from these estimates, our provision for income taxes could be materially impacted.

Effective January 1, 2007, we adopted FASB Interpretation No. 48, "*Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109*", or FIN 48, which clarifies the accounting and disclosure for uncertainty in tax positions, as defined. FIN 48 requires us to perform a two-step evaluation of all tax positions, ensuring that these tax return positions meet the "more-likely than not" recognition threshold and can be measured with sufficient precision to determine the benefit recognized in the financial statements. These evaluations provide us with a comprehensive model for how we should recognize, measure, present, and disclose in our financial statements certain tax

positions that we have taken or expect to take on income tax returns. Management estimated that as of December 31, 2006, there was an uncertain tax position totaling approximately $100,000 relating to our tax credit carryforwards. As a result, we reduced our deferred tax assets and the associated valuation allowance by approximately $100,000 as of January 1, 2007, the adoption date of FIN 48. There have been no other activities impacting FIN 48 reserves during the year ended December 31, 2007.

Accounting for Stock-Based Compensation

Effective January 1, 2006, we adopted SFAS No. 123(R) using the modified prospective method and began reflecting the stock-based compensation expense determined under fair value based methods in our statement of operations rather than as pro forma disclosure in our notes to the financial statements. Under this transition method, the compensation cost recognized beginning January 1, 2006 includes compensation cost for (i) all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123, "*Accounting for Stock-Based Compensation*", or SFAS No. 123, and (ii) all share based payments granted or modified subsequent to January 1, 2006 based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123(R). Compensation cost is generally recognized ratably over the requisite service period. Prior period amounts have not been restated. We use the Black-Scholes option pricing model for determining the fair value of our stock options and amortize our stock-based compensation expense using the straight-line method.

Goodwill and Other Intangible Assets

As result of our acquisition of substantially all of the assets of EyeTel on December 26, 2007, there was approximately $5.8 million of goodwill and $2.8 million of other intangible assets on our balance sheet at December 31, 2007. We will amortize intangible assets using the straight-line method over their estimated economic lives, which is currently estimated to be five years. Determining the economic lives of acquired intangible assets requires us to make significant judgment and estimates, and can materially impact our operating results.

SFAS No. 142, "*Goodwill and Other Intangible Assets*", or SFAS No. 142, requires us to assess the realizability of goodwill annually, as well as whenever events or changes in circumstances suggest that the carrying amount may not be recoverable. The Company's ability to realize the value of the goodwill will depend on the future cash flows of the business. If the Company is not able to realize the value of goodwill, the Company may be required to incur material charges relating to the impairment of goodwill.

We are required to perform impairment tests under SFAS No. 142 annually and whenever events or changes in circumstances suggest that the carrying value of an asset may not be recoverable. For the acquisition, various analyses, assumptions and estimates were made at the time of the acquisition specifically regarding product development, market conditions and expected cash flows that were used to determine the valuation of goodwill and intangibles.

When we perform impairment tests in future years, changes in forecasts and estimates from those used at the acquisition date could result in impairment charges.

Other Long-Lived Assets

We periodically evaluate long-lived assets for potential impairment under SFAS No. 144. We plan to perform these evaluations whenever events or changes in circumstances suggest that the carrying value of an asset or group of assets is not recoverable. If we believe an indicator of potential impairment exists, we test to determine whether the impairment recognition criteria in SFAS No. 144

have been met. In evaluating long-lived assets for potential impairment, we will make several significant estimates and judgments, including:

- determining the appropriate grouping of assets at the lowest level for which cash flows are available;
- estimating future cash flows associated with the asset or group of assets; and
- determining an appropriate discount rate to use in the analysis.

If different estimates and judgments are used, the amount and timing of impairments could be affected.

New Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board, or FASB, issued SFAS No. 141 (Revised 2007), "*Business Combinations*", or SFAS No. 141R. SFAS No. 141R will significantly change the accounting for business combinations. Under SFAS No. 141R, an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. SFAS No. 141R will change the accounting treatment for certain specific acquisition related items including: (1) expensing acquisition related costs as incurred; (2) valuing noncontrolling interests at fair value at the acquisition date; and (3) expensing restructuring costs associated with an acquired business. SFAS No. 141R also includes a substantial number of new disclosure requirements. SFAS No. 141R is to be applied prospectively to business combinations for which the acquisition date is on or after January 1, 2009. We expect SFAS No. 141R will have an impact on our accounting for future business combinations once adopted but the effect is dependent upon the acquisitions that are made in the future.

In February 2007, the FASB issued SFAS No. 159, "*The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115*", or SFAS No. 159. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We believe that our adoption of SFAS No. 159 will not have a material impact on our financial position, results of operations or cash flows.

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements*", or SFAS No. 157. SFAS No. 157 defines fair value in numerous accounting pronouncements, establishes a framework for measuring fair value in generally accepted accounting principles ("GAAP") and expands disclosures related to the use of fair value measures in financial statements. SFAS No. 157 does not expand the use of fair value measures in financial statements, but standardizes its definition and guidance in GAAP. SFAS No. 157 emphasizes that fair value is a market-based measurement and not an entity-specific measurement based on an exchange transaction in which the entity sells an asset or transfers a liability (exit price). SFAS No. 157 establishes a fair value hierarchy from observable market data as the highest level to fair value based on an entity's own fair value assumptions as the lowest level. SFAS No. 157 was to be effective for our financial statements issued in 2008. In February 2008, the FASB issued FASB Statement of Position, or FSP, No. 157-2 "*Partial Deferral of the Effective Date of Statement 157,*" or FSP No. 157-2, which delays the effective date of SFAS No. 157 for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financials statements on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008. We have not yet determined the impact that the adoption of SFAS No. 157 will have on our financial position, results of operations or its cash flows.

Subsequent Events

Joint Venture with Cyberkinetics

In February 2008, we entered into a Collaboration Agreement and Operating Agreement with Cyberkinetics to develop and commercialize products for the treatment of peripheral nerve injury and formed PNIR (Peripheral Nerve Injury Repair) LLC, a joint venture with 50% ownership held by us and 50% ownership held by Cyberkinetics.

Under the terms of the joint venture, we have agreed to fund the initial $2.0 million in product development costs and have agreed to share equally in all costs in excess of the initial $2.0 million. Cyberkinetics has agreed to contribute technology, know-how and intellectual property, primarily relating to their Andara OFS technology, to the joint venture.

We obtained sales and marketing rights and Cyberkinetics obtained commercial manufacturing rights to any products commercialized under the joint venture. Each party will charge the joint venture at cost for all expenses incurred in connection with their respective commercialization activities. Based on the initial ownership of the joint venture, we will equally split profits and losses realized from the joint venture with Cyberkinetics.

Lease Agreement

In February 2008, we amended the Lease Agreement dated October 18, 2000 between Fourth Avenue LLC and us for office and engineering laboratory space. The amendment extends the term of the lease, currently scheduled to expire on March 31, 2009, through March 31, 2013. Base rent for the period April 2009 through March 2013 will be reduced from the current level of $930,000 annually to a range of $675,000 to $765,000 annually.

In connection with the amendment of the lease, the amount of the irrevocable letter of credit required to be maintained by us for the benefit of the lessor will be reduced from $1,430,000 to $400,000. The letter of credit must be secured by a certificate of deposit in an amount equal to 102% of the letter of credit as security.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

The statements contained in this annual report on Form 10-K, including under the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and other sections of this annual report, include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including, without limitation, statements regarding our or our management's expectations, hopes, beliefs, intentions or strategies regarding the future. The words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "expect," "plan" and similar expressions may identify forward-looking statements, but the absence of these words does not mean that a statement is not forward-looking. The forward-looking statements contained in this annual report are based on our current expectations and beliefs concerning future developments and their potential effects on us. There can be no assurance that future developments affecting us will be those that we have anticipated. These forward-looking statements involve a number of risks, uncertainties (some of which are beyond our control) or other assumptions that may cause actual results or performance to be materially different from those expressed or implied by these forward-looking statements. These risks and uncertainties include, but are not limited to, those factors described in the section titled "Risk Factors." Should one or more of these risks or uncertainties materialize, or should any of our assumptions prove incorrect, actual results may vary in material respects from those projected in these forward-looking statements. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required under applicable securities laws.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We do not use derivative financial instruments in our investment portfolio and have no foreign exchange contracts. Our financial instruments consist of cash, cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses. We consider investments that, when purchased, have a remaining maturity of 90 days or less to be cash equivalents. The primary objectives of our investment strategy are to preserve principal, maintain proper liquidity to meet operating needs, and maximize yields. To minimize our exposure to an adverse shift in interest rates, we invest mainly in cash equivalents and short-term investments with a maturity of 12 months or less and maintain an average maturity of twelve months or less. We do not believe that a notional or hypothetical 10% change in interest rate percentages would have a material impact on the fair value of our investment portfolio or our interest income.

Item 8. Financial Statements and Supplementary Data

The information required by this item may be found on pages F-1 through F-30 of this Form 10-K with the exception of the unaudited quarterly financial information which is presented below:

	Year Ended December 31, 2007				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Revenues	$ 11,757,786	11,475,509	11,290,004	$ 10,098,912	$ 44,622,211
Gross margin	$ 8,663,168	8,407,874	8,241,990	$ 7,247,381	$ 32,560,413
Net loss attributable to common shareholders	$ (1,377,282)	(1,290,991)	(3,570,925)	$ (2,139,276)	$ (8,378,474)
Net loss per common share:					
Basic	$ (0.11)	(0.10)	(0.28)	$ (0.17)	$ (0.66)
Diluted	$ (0.11)	(0.10)	(0.28)	$ (0.17)	$ (0.66)
Weighted average shares used to compute net loss per common share:					
Basic	12,605,431	12,611,880	12,624,465	12,693,209	12,628,310
Diluted	12,605,431	12,611,880	12,624,465	12,693,209	12,628,310

	Year Ended December 31, 2006				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Revenues	$ 11,823,275	$ 13,970,050	$ 15,261,251	$ 14,195,140	$ 55,249,716
Gross margin	$ 8,943,362	$ 10,592,584	$ 11,525,299	$ 10,630,417	$ 41,691,662
Net income (loss) attributable to common shareholders	$ (102,662)	$ 1,233,700	$ 2,104,630	$ 1,032,138	$ 4,267,806
Net income (loss) per common share:					
Basic	$ (0.01)	$ 0.10	$ 0.17	$ 0.08	$ 0.34
Diluted	$ (0.01)	$ 0.09	$ 0.16	$ 0.08	$ 0.33
Weighted average shares used to compute net income (loss) per common share:					
Basic	12,414,479	12,485,205	12,539,709	12,583,825	12,501,742
Diluted	12,414,479	13,137,867	13,095,430	12,926,449	13,097,891

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

There have been no changes in or disagreements with accountants on accounting and financial disclosure matters in the last fiscal year.

Item 9A. Controls and Procedures

(a)

Evaluation of disclosure controls and procedures.

Our management carried out an evaluation, with the participation of our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of December 31, 2007. Our disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and

communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosures.

Based upon the evaluation described above, our Chief Executive Officer and Chief Financial Officer have concluded that they believe that our disclosure controls and procedures are effective, as of the end of the period covered by this report, in providing reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and is accumulated and communicated to the issuer's management, including its principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosures. We continue to review and document our disclosure controls and procedures, including our internal controls over financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our business.

(b)

Management's Report on Internal Control Over Financial Reporting.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2007 based on the criteria in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on our evaluation under the framework in *Internal Control Integrated Framework* issued by the COSO, our management concluded that our internal control over financial reporting was effective as of December 31, 2007.

Management has excluded EyeTel from our assessment of internal control over financial reporting as of December 31, 2007 because it was acquired by us in a purchase business combination during the year ended December 31, 2007. The total assets and total revenues related to the acquisition of EyeTel represent 4% and 0%, respectively, of the related financial statement amounts as of and for the year ended December 31, 2007.

The effectiveness of our internal control over financial reporting as of December 31, 2007, has been audited by PricewaterhouseCoopers LLP, an independent registered accounting firm, as stated in their report which is included herein.

(c)

Changes in internal control over financial reporting.

There have been no changes to the Company's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the quarter ended December 31, 2007 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The response to this item is contained in our Proxy Statement relating to our 2008 Annual Meeting of Stockholders (the "Proxy Statement") and is incorporated herein by reference.

Item 11. Executive Compensation

The response to this item is incorporated herein by reference from the discussion responsive thereto in the Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The response to this item is incorporated herein by reference from the discussion responsive thereto in the Proxy Statement.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The response to this item is incorporated herein by reference from the discussion responsive thereto in the Proxy Statement.

Item 14. Principal Accountant Fees and Services

The response to this item is incorporated herein by reference from the discussion responsive thereto in the Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a)

1. *Financial Statements*

The financial statements are listed in the accompanying index to financial statements on page F-1.

2. *Financial Statement Schedule*

The Schedule on page S-1 is filed as part of this report.

3. *Exhibit Index:*

Exhibit Number	Description
2.1	Asset Purchase Agreement by and among NeuroMetrix, Inc., EyeTel Imaging, Inc. and EyeTel Reading Center, LLC, dated as of December 26, 2007 (9)
3.1	Second Amended and Restated By-laws of NeuroMetrix, Inc. (10)
3.2	Third Amended and Restated Certificate of Incorporation of NeuroMetrix, Inc. (10)
3.3	Certificate of Designations for Series A Junior Cumulative Preferred Stock, par value $0.001 per share (7)
3.4	Amendment No. 1 to Second Amended and Restated Bylaws of NeuroMetrix, Inc. (8)
4.1	Specimen certificate for shares of common stock (1)
4.2	Shareholder Rights Agreement, dated as of March 7, 2007, between NeuroMetrix, Inc. and American Stock Transfer & Trust Company, as Rights Agent (7)
10.1	Lease Agreement dated October 18, 2000 between Fourth Avenue LLC and NeuroMetrix, Inc. (1)
10.2	Amended and Restated 1996 Stock Option/Restricted Stock Plan (1)
10.3	Amended and Restated 1998 Equity Incentive Plan (1)
10.4	First Amendment to Amended and Restated 1998 Equity Incentive Plan (1)
10.5	Amended and Restated 2004 Stock Option and Incentive Plan (2)
10.6	2004 Employee Stock Purchase Plan (1)
10.7	Form of Indemnification Agreement between NeuroMetrix, Inc. and each of its directors (1)
10.8	Employment Agreement, dated June 21, 2004, by and between NeuroMetrix, Inc. and Shai N. Gozani, M.D., Ph.D. (1)
10.9	Letter Agreement, dated June 19, 2002, by and between NeuroMetrix, Inc. and Gary L. Gregory (1)
10.10	NeuroMetrix, Inc. Stock Option Agreements (1998 Plan) dated as of July 1, 2002 and April 8, 2004 by and between NeuroMetrix, Inc. and Gary L. Gregory (1)
10.11	NeuroMetrix, Inc. Confidentiality and Non-Compete Agreement, dated as of June 28, 2002, by and between Gary L. Gregory and NeuroMetrix, Inc. (1)
10.12	NeuroMetrix, Inc. Confidentiality & Non-Compete Agreement dated as of June 21, 2004, by and between Shai N. Gozani, M.D., Ph.D. and NeuroMetrix, Inc. (1)
10.13	NeuroMetrix, Inc. Non-Statutory Stock Option Agreement (1998 Plan) dated as of June 21, 2004, by and between Shai N. Gozani M.D., Ph.D., and NeuroMetrix, Inc. (1)
10.14	Second Amendment to Amended and Restated 1998 Equity Incentive Plan (1)
10.15	NeuroMetrix, Inc. Non-Statutory Stock Option Agreement (1998 Plan) dated as of June 21, 2004 by and between Gary Gregory and NeuroMetrix, Inc. (1)
10.16	Indemnification Agreement dated June 21, 2004, by and between Shai N. Gozani, M.D., Ph.D., and NeuroMetrix, Inc. (1)
10.17	NeuroMetrix, Inc. Confidentiality & Non-Compete Agreement, dated as of May 1, 2000, by and between Michael Williams and NeuroMetrix, Inc. (1)

10.18	NeuroMetrix, Inc. Confidentiality & Non-Compete Agreement, dated as of October 13, 1998, by and between Guy Daniello and NeuroMetrix Inc. (1)
10.19	Form of Incentive Stock Option Agreement, under the NeuroMetrix, Inc. 2004 Stock Option And Incentive Plan (3)
10.20	Form of Non-Qualified Stock Option Agreement For Company Employees, under the NeuroMetrix, Inc. 2004 Stock Option And Incentive Plan (3)
10.21	Form of Non-Qualified Stock Option Agreement For Non-Employee Directors, under the NeuroMetrix, Inc. 2004 Stock Option And Incentive Plan (3)
10.22	Letter Agreement, dated February 7, 2005, by and between NeuroMetrix, Inc. and W. Bradford Smith (4)
10.23	Form of Incentive Stock Option Agreement, under the NeuroMetrix, Inc. 2004 Stock Option and Incentive Plan, by and between NeuroMetrix, Inc. and W. Bradford Smith (4)
10.24	NeuroMetrix, Inc. Confidentiality & Non-Compete Agreement, dated as of February 7, 2005, by and between W. Bradford Smith and NeuroMetrix, Inc. (4)
10.25	Director Compensation Arrangements (5)
10.26	Manufacturing and Supply Agreement, dated as of August 2, 2006, by and between Parlex Polymer Flexible Circuits, Inc. and NeuroMetrix, Inc. (6)
*23.1	Consent of PricewaterhouseCoopers LLP
*31.1	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
*31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
*32	Certification of Principal Executive Officer and Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

*

Filed herewith.

Portions of this exhibit have been omitted pursuant to a request for confidential treatment.

(1)

Incorporated herein by reference to NeuroMetrix, Inc.'s Registration Statement on Form S-1 (Registration No. 333-115440).

(2)

Incorporated herein by reference to NeuroMetrix, Inc.'s Current Report on Form 8-K filed on May 26, 2006 (File No. 000-50856).

(3)

Incorporated herein by reference to NeuroMetrix, Inc.'s Quarterly Report on Form 10-Q filed on November 15, 2004 (File No. 000-50856).

(4)

Incorporated herein by reference to NeuroMetrix, Inc.'s Current Report on Form 8-K filed on February 11, 2005 (File No. 000-50856).

(5)

Incorporated herein by reference to NeuroMetrix, Inc.'s Annual Report on Form 10-K filed on March 16, 2006 (File No. 000-50856).

(6)

Incorporated herein by reference to NeuroMetrix, Inc.'s Current Report on Form 8-K filed on August 2, 2006 (File No. 000-50856).

(7)

Incorporated herein by reference to NeuroMetrix, Inc.'s Current Report on Form 8-K filed on March 8, 2007 (File No. 000-50856).

(8)

Incorporated herein by reference to NeuroMetrix, Inc.'s Current Report on Form 8-K filed on September 17, 2007 (File No. 000-50856).

(9) Incorporated herein by reference to NeuroMetrix, Inc.'s Current Report on Form 8-K filed on December 28, 2007 (File No. 000-50586).

(10) Incorporated herein by reference to NeuroMetrix, Inc.'s Registration Statement on Form S-8 (Registration No. 333-118059).

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NEUROMETRIX, INC.

By: /s/ SHAI N. GOZANI, M.D. PH.D.

Shai N. Gozani, M.D. Ph.D.
Chairman, President and Chief Executive Officer

Date: March 14, 2008

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant on March 14, 2008 in the capacities indicated below.

Name	Title	Date
/s/ SHAI N. GOZANI, M.D., PH. D. Shai N. Gozani, M.D., Ph. D.	Chairman, President and Chief Executive Officer (Principal Executive Officer)	
/s/ W. BRADFORD SMITH W. Bradford Smith	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	
/s/ DAVID E. GOODMAN, M.D. David E. Goodman, M.D.	Director	
/s/ ALLEN J. HINKLE, M.D. Allen J. Hinkle, M.D.	Director	
/s/ CHARLES R. LAMANTIA Charles R. LaMantia	Director	
/s/ W. MARK LORTZ W. Mark Lortz	Director	

INDEX TO FINANCIAL STATEMENTS

NeuroMetrix, Inc.

Years ended December 31, 2007, 2006 and 2005

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of NeuroMetrix, Inc.:

In our opinion, the accompanying balance sheets and the related statements of operations, statements of changes in stockholders' equity, and statements of cash flows present fairly, in all material respects, the financial position of NeuroMetrix, Inc. at December 31, 2007 and December 31, 2006, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on these financial statements, on the financial statement schedule and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 2 to the financial statements, the Company changed the manner in which it accounts for share-based compensation in 2006.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As described in Management's Report on Internal Control over Financial Reporting, management has excluded EyeTel Imaging, Inc. from its assessment of internal control over financial reporting as of December 31, 2007 because it was acquired by the Company in a purchase business combination during the year ended December 31, 2007. We have also excluded EyeTel Imaging, Inc. from our audit of internal control over financial reporting. Total assets and total revenues related to the acquisition of EyeTel Imaging, Inc. represent 4.0% and 0.0%, respectively, of the related financial statement amounts as of and for the year ended December 31, 2007.

/s/ PricewaterhouseCoopers LLP

Boston, Massachusetts
March 14, 2008

NeuroMetrix, Inc.

Balance Sheets

	December 31,	
	2007	**2006**
Assets		
Current assets:		
Cash and cash equivalents	$ 7,097,239	$ 7,909,778
Short-term held-to-maturity investments	22,621,741	32,410,685
Restricted cash	45,000	
Accounts receivable, net of allowance for doubtful accounts of $906,000 and $900,000 at December 31, 2007 and 2006, respectively	5,731,697	7,698,550
Inventories	5,354,338	3,633,389
Prepaid expenses and other current assets	710,159	761,400
Current portion of deferred costs	464,061	370,013
Total current assets	42,024,235	52,783,815
Restricted cash	1,458,598	1,458,598
Fixed assets, net	2,973,718	1,115,436
Long-term available-for-sale investment	1,058,255	
Goodwill	5,833,464	
Other intangible assets	2,800,000	
Deferred costs	226,304	348,430
Total assets	$ 56,374,574	$ 55,706,279
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 2,627,889	$ 2,766,650
Accrued compensation	2,127,546	2,460,328
Accrued expenses	2,308,563	4,275,983
Current portion of deferred revenue	1,643,026	1,386,867
Current portion of capital lease obligation	12,900	
Total current liabilities	8,719,924	10,889,828
Deferred revenue	891,958	1,335,138
Capital lease obligation net of current portion	18,275	
Other long-term liabilities	14,546	72,727
Total liabilities	9,644,703	12,297,693
Commitments and contingencies (Note 9)		
Stockholders' equity		
Preferred stock, $0.001 par value, 5,000,000 shares authorized, none outstanding		
Common stock, $0.0001 par value; 50,000,000 authorized; 13,690,134 and 12,601,224 shares issued and outstanding at December 31, 2007 and 2006, respectively	1,369	1,260
Additional paid-in capital	110,235,835	97,205,145
Deferred compensation		(110,705)
Accumulated deficit	(62,065,588)	(53,687,114)
Accumulated other comprehensive loss	(1,441,745)	
Total stockholders' equity	46,729,871	43,408,586
Total liabilities and stockholders' equity	$ 56,374,574	$ 55,706,279

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

NeuroMetrix, Inc.

Statements of Operations

	Years Ended December 31,		
	2007	**2006**	**2005**
Revenues:			
Diagnostic device	$ 4,254,011	$ 7,538,320	$ 4,221,311
Biosensor	39,413,265	47,711,396	30,076,822
Other	954,935		
Total revenues	44,622,211	55,249,716	34,298,133
Cost of revenues	12,061,798	13,558,054	8,858,094
Gross margin	32,560,413	41,691,662	25,440,039
Operating expenses:			
Research and development	4,891,937	5,010,513	3,820,624
Sales and marketing	22,963,840	22,013,682	14,150,157
General and administrative	14,834,073	11,805,062	8,021,783
Total operating expenses	42,689,850	38,829,257	25,992,564
Income (loss) from operations	(10,129,437)	2,862,405	(552,525)
Interest income	1,750,963	1,598,401	838,825
Interest expense			(2,042)
Income (loss) before provision for income taxes	(8,378,474)	4,460,806	284,258
Provision for income taxes		193,000	35,000
Net income (loss)	$ (8,378,474)	$ 4,267,806	$ 249,258
Net income (loss) per common share:			
Basic	$ (0.66)	$ 0.34	$ 0.02
Diluted	$ (0.66)	$ 0.33	$ 0.02
Weighted average shares used to compute net income (loss) per common share:			
Basic	12,628,310	12,501,742	12,152,139
Diluted	12,628,310	13,097,891	12,986,365
Comprehensive income (loss):			
Net income (loss)	$ (8,378,474)	$ 4,267,806	$ 249,258
Unrealized loss on available-for-sale investment	(1,441,745)		
Comprehensive income (loss)	$ (9,820,219)	$ 4,267,806	$ 249,258

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

NeuroMetrix, Inc.

Statements of Changes in Stockholders' Equity

	Common Stock						
	Number of Shares	Amount	Additional Paid-In Capital	Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
Balance at December 31, 2004	12,034,650	$ 1,203	$ 92,278,379	$ (745,086)	$ (58,204,178)	$	33,330,318
Issuance of stock upon exercise of stock options and warrants	317,361	32	512,825				512,857
Compensation expense associated with stock options			120,272				120,272
Adjustment to deferred compensation associated with terminated employees			(33,405)	33,405			
Amortization of deferred compensation				286,058			286,058
Issuance of common stock under employee stock purchase plan	23,265	3	299,297				299,300
Income tax effect of the exercise of stock options			35,000				35,000
Net income					249,258		249,258
Balance at December 31, 2005	12,375,276	1,238	93,212,368	(425,623)	(57,954,920)		34,833,063
Issuance of stock upon exercise of stock options	202,808	20	1,180,637				1,180,657
Stock-based compensation expense			2,403,222				2,403,222
Adjustment to deferred compensation associated with terminated employees			(65,503)	65,503			
Amortization of deferred compensation				249,415			249,415
Issuance of common stock under employee stock purchase plan	23,140	2	394,621				394,623
Income tax effect of the exercise of			79,800				79,800

	Common Stock							
stock options								
Net income					4,267,806		4,267,806	
Balance at December 31, 2006	12,601,224	1,260	97,205,145	(110,705)	(53,687,114)		43,408,586	
Issuance of stock upon exercise of stock options	5,957	1	24,099				24,100	
Stock-based compensation expense			2,976,059		986.6	2.5	984.1	
Individual Disability	558.3	3.5	1,155.7	124.4	5.2	1,838.4	104.3	1,734.1
Voluntary Benefits	1,298.4	8.1	48.9	73.2	0.5	1,420.5	29.2	1,391.3
Unum US Segment	1,929.0	12.1	8,728.1	967.8	39.5	11,624.9	202.6	11,422.3
Unum UK Segment	24.9	0.1	2,286.0	171.7	10.0	2,482.6	130.1	2,352.5
Colonial Life Segment	1,577.6	9.9	274.1	134.1	1.7	1,985.8	13.9	1,971.9
Individual Disability	859.3	5.4	10,346.8	281.9	43.3	11,488.0	1,545.0	9,943.0
Long-term Care	5,791.4	36.3	865.7	94.8	3.9	6,751.9	42.6	6,709.3
Other	5,783.8	36.2	234.4	150.2	1.6	6,168.4	4,915.2	1,253.2
Closed Block Segment	12,434.5	77.9	11,446.9	526.9	48.8	24,408.3	6,502.8	17,905.5
Subtotal	$15,966.0	100.0%	$ 22,735.1	$1,800.5	100.0%	40,501.6	6,849.4	33,652.2
Adjustment to Reserves for Unrealized Gain on Securities						4,108.5	263.8	3,844.7
Consolidated						$44,610.1	$7,113.2	$37,496.9

Key Assumptions

The calculation of policy and claim reserves involves numerous assumptions, but the primary assumptions used to calculate reserves are (1) the discount rate, (2) the claim resolution rate, and (3) the claim incidence rate for policy reserves and IBNR claim reserves. Of these assumptions, our discount rate and claim resolution rate assumptions have historically had the most significant effects on our level of reserves because many of our product lines provide benefit

payments over an extended period of time.

1. The discount rate, which is used in calculating both policy reserves and incurred and IBNR claim reserves, is the interest rate that we use to discount future claim payments to determine the present value. A higher discount rate produces a lower reserve. If the discount rate is higher than our future investment returns, our invested assets will not earn enough investment income to support our future claim payments. In this case, the reserves may eventually be insufficient. We set our assumptions based on our current and expected future investment yield of the assets supporting the reserves, considering current and expected future market conditions. If the investment yield on new investments that are purchased is below or above the investment yield of the existing investment portfolio, it is likely that the discount rate assumption on claims will be established to reflect the effect of the new investment yield.

2. The claim resolution rate, used for both policy reserves and incurred and IBNR claim reserves, is the probability that a disability or long-term care claim will close due to recovery or death of the insured. It is important because it is used to estimate how long benefits will be paid for a claim. Estimated resolution rates that are set too high will result in reserves that are lower than they need to be to pay the claim benefits over time. Claim resolution assumptions involve many factors, including the cause of disability, the policyholder's age, the type of contractual benefits provided, and the time since initially becoming disabled. We primarily use our own claim experience to develop our claim resolution assumptions. These assumptions are established for the probability of death and the probability of recovery from disability. Our studies review actual claim resolution experience over a number of years, with more weight placed on our experience in the more recent years. We also consider any expected future changes in claim resolution experience.

3. The incidence rate, used for policy reserves and IBNR claim reserves, is the rate at which new claims are submitted to us. The incidence rate is affected by many factors, including the age of the insured, the insured's occupation or industry, the benefit plan design, and certain external factors such as consumer confidence and levels of unemployment. We establish our incidence assumption using a historical review of actual incidence results along with an outlook of future incidence expectations.

Establishing reserve assumptions is complex and involves many factors. Reserves, particularly for policies offering insurance coverage for long-term disabilities and long-term care, are dependent on numerous assumptions other than just those presented in the preceding discussion. The impact of internal and external events, such as changes in claims operational procedures, economic trends such as the rate of unemployment and the level of consumer confidence, the emergence of new diseases, new trends and developments in medical treatments, and legal trends and legislative changes, including changes to social security and other government-based welfare benefits programs which provide policy benefit offsets, among other factors, will influence claim incidence rates, claim resolution rates, and claim costs. In addition, for policies offering coverage for disability or long-term care at advanced ages, the level and pattern of mortality rates at advanced ages will impact overall benefit costs. Reserve assumptions differ by product line and by policy type within a product line. Additionally, in any period and over time, our actual experience may have a positive or negative variance from our long-term assumptions, either singularly or collectively, and these variances may offset each other. We test the overall adequacy of our reserves using all assumptions and with a long-term view of our expected experience over the life of a block of business rather than test just one or a few assumptions independently that may be aberrant over a short period of time. Therefore, it is not possible to bifurcate the assumptions to evaluate the sensitivity of a change in each assumption, but rather in the aggregate by product line. The following section presents an overview of our trend analysis for key assumptions and the results of variability in our assumptions, in aggregate, for the reserves which we believe are reasonably possible to have a material impact on our future financial results if actual claims yield a materially different amount than what we currently expect and have reserved for, either favorable or unfavorable.

Trends in Key Assumptions

Generally, we do not expect our mortality and morbidity claim incidence trends or our persistency trends to change significantly in the short-term, and to the extent that these trends do change, we expect those changes to be gradual over a longer period of time. We have historically experienced an increase in our group long-term disability morbidity claim incidence trends during and following a recessionary period, particularly in our Unum US operations. During 2014, claim incidence rates for Unum US group long-term disability were stable relative to the prior year, continuing to benefit from the gradual improvement in the economy. During 2013, claim incidence rates for Unum US group long-term disability improved slightly compared to the slightly elevated level of incidence rates in 2012. We expect that claim incidence trends for Unum US group long-term disability may continue to somewhat follow general economic conditions and demographics of the general U.S. workforce.

During 2014, our claim incidence rates for our Closed Block long-term care line of business improved slightly relative to the levels of 2013 and 2012, when we experienced claim incidence rates higher than the long-term assumptions we established at the time of loss recognition in 2011. We undertook a thorough review of our reserve assumptions related to our long-term care line of business during 2014 and updated our reserves using best estimate assumptions as of the date of the review. See "2014 Long-term Care Reserve Increase" contained in this Item 7.

Interest rates improved somewhat during 2013 and early 2014 before returning to levels well below historical norms in the latter part of 2014, and the assumptions we used to discount our reserves during these periods generally trended downward slightly for all segments and product lines. Reserve discount rate assumptions for new policies and new claims are adjusted to reflect our current and expected net investment returns. Changes in our average discount rate assumptions tend to occur gradually over a longer period of time because of the long-duration investment portfolios

which support the reserves for the majority of our lines of business.

Claim resolution rates have a greater chance of significant variability in a shorter period of time than our other reserve assumptions. These rates are reviewed on a quarterly basis for the death and recovery components separately. Claim resolution rates in our Unum US group and individual long-term disability product lines and our Closed Block individual disability product line have over the last several years exhibited some variability. Relative to the resolution rate we expect to experience over the life of the block of business, actual quarterly rates during 2013 and 2014 have varied by +3 and -2 percent in our Unum US group long-term disability line of business, between +10 and -13 percent in our Unum US individual disability line of business, and between +7 and -6 percent in our Closed Block individual disability line of business. Claim resolution rates are very sensitive to operational and environmental changes and can be volatile over short periods of time. Throughout the period 2012 to 2014, our claim resolution rates were fairly consistent with or slightly favorable to our long-term assumptions. Our claim

resolution rate assumption used in determining reserves is our expectation of the resolution rate we will experience over the life of the block of business and will vary from actual experience in any one period, both favorably and unfavorably.

Regarding experience for our older age, longer duration disabled claimants in our Closed Block individual disability line of business, the claim resolution rates, primarily as pertaining to life expectancy of the insured, showed a reduction in the number of deaths at these older ages during 2014, which we believe is temporary in nature. During 2013 and 2012, mortality assumptions remained relatively consistent with the assumptions that we updated in 2011 for this particular claim block.

We monitor and test our reserves for adequacy relative to all of our assumptions in the aggregate. In our estimation, scenarios based on reasonably possible variations in each of our reserve assumptions, when modeled together in aggregate, could produce potential results as illustrated in the chart below. The major contributor to the variance for both the Unum US group long-term disability line of business and the Closed Block individual disability line of business is the claim resolution rate.

	Potential impact, positive or negative, of variations in reserve assumptions on our December 31, 2014 claim reserve balance (in millions of dollars)	
Unum US group long-term disability	3.6%	$250
Closed Block individual disability	2.5%	$245

In addition, we consider variability in our reserve assumptions related to long-term care policy reserves. These reserves are held under the gross premium valuation method with assumptions established as of December 31, 2014, the date of loss recognition. Assumptions for policy reserves do not change after the date of loss recognition unless reserves are again determined to be deficient. As such, positive developments will result in the accumulation of reserve margin, while adverse developments would result in an additional reserve charge. Policy reserves for long-term care are based upon a number of key assumptions, and each assumption has various factors which may impact the long-term outcome. Key assumptions with respect to morbidity, mortality, persistency, interest rates, and future premium rate increases must incorporate extended views of expectations for many years into the future. Reserves are highly sensitive to these estimates. For example, a 25 basis point change in the assumed discount rate over the lifetime of this business would impact reserves by approximately $475 million, assuming all other factors held constant.

Key assumptions and related impacts are also heavily interrelated in both their outcome and in their effects on reserves. For example, changes in the view of morbidity and mortality might be mitigated by either potential future premium rate increases and/or morbidity improvements due to general improvement in health and/or medical breakthroughs. There is potentially a wide range of outcomes for each assumption and in totality.

We believe that these ranges provide a reasonable estimate of the possible changes in reserve balances for those product lines where we believe it is possible that variability in the assumptions, in the aggregate, could result in a material impact on our reserve levels, but we record our reserves based on our long-term best estimate. Because these product lines have long-term claim payout periods, there is a greater potential for significant variability in claim costs, either positive or negative. We closely monitor emerging experience and use these results to inform our view of long-term assumptions.

Deferred Acquisition Costs (DAC)

We defer incremental direct costs associated with the successful acquisition of new or renewal insurance contracts and amortize (expense) these costs over the life of the related policies. Deferred costs include certain commissions, other

agency compensation, selection and policy issue expenses, and field expenses. Acquisition costs that do not vary with the production of new business, such as commissions on group products which are generally level throughout the life of the policy, are excluded from deferral.

Approximately 83.7 percent of our DAC relates to non interest-sensitive products, and we amortize DAC for these products in proportion to the premium income we expect to receive over the life of the policies. DAC related to interest-sensitive policies is amortized over the lives of the policies in relation to the present value of estimated gross profits from surrender charges, mortality margins, investment returns, and expense margins. Key assumptions used in developing the future amortization of DAC are persistency, premium income, and for our interest-sensitive products, mortality margins and investment returns. We use our own historical experience and expectation of the future performance of our businesses in determining our assumptions. For non-interest sensitive products, the estimated premium income in the early years of the amortization period is generally higher than in the later years due to the anticipated cumulative effect of policy persistency in the early years, which results in a greater proportion of the costs being amortized in the early years of the life of the policy. During 2014, our key assumptions

used to develop the future amortization of acquisition costs deferred during 2014 did not change materially from those used in 2013. Generally, we do not expect our key assumptions to change significantly in the short-term, and to the extent that these trends do change, we expect those changes to be gradual over a longer period of time.

The following are our current assumptions regarding the length of our amortization periods, the approximate DAC balance that remains at the end of years 3, 10, and 15 as a percentage of the cost initially deferred, and our DAC balances as of December 31, 2014 and 2013.

	Amortization Period	Balance Remaining as a % of Initial Deferral			DAC Balances at December 31	
		Year 3	Year 10	Year 15	2014	2013
Unum US					(in millions of dollars)	
Group Disability	6	30%	0%	0%	$69.8	$55.9
Group Life and Accidental Death & Dismemberment	6	31%	0%	0%	59.8	49.9
Supplemental and Voluntary:						
Individual Disability	20	71%	44%	21%	423.6	433.4
Voluntary Benefits	20	58%	23%	8%	543.3	512.3
Unum UK						
Group Long-term Disability	3	0%	0%	0%	5.1	5.1
Group Life	3	0%	0%	0%	1.3	1.2
Supplemental	20	57%	17%	7%	24.0	28.0
Colonial Life						
Accident, Sickness, and Disability	15	46%	12%	2%	378.2	350.6
Life	25	70%	33%	16%	215.2	218.7
Cancer and Critical Illness	19	59%	26%	10%	181.0	174.1
Totals					$1,901.3	$1,829.2

Amortization of DAC is adjusted to reflect actual experience for assumptions which deviate compared to the anticipated experience. Any deviations from projections may result in a change to the rate of amortization in the period such events occur. As an example, for our non-interest sensitive products, we may experience accelerated amortization if policies terminate earlier than projected, or we may experience a slower rate of amortization if policies persist longer than projected. Our actual experience has not varied materially from our assumptions during the last three years.

See Note 1 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of our DAC accounting policy.

Fair Value of Investments

All of our fixed maturity securities are classified as available-for-sale and are reported at fair value. Our derivative financial instruments, including certain derivative instruments embedded in other contracts, are reported as either assets or liabilities and measured at fair value. We hold an immaterial amount of equity securities, which are also reported at fair value.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and therefore represents an exit price, not an entry price. The exit price objective applies regardless of our intent and/or ability to sell the asset or transfer the liability at the measurement date. We generally use valuation techniques consistent with the market approach, and to a lesser extent, the income approach. The market approach uses prices and other relevant information from market transactions involving identical or comparable assets or liabilities and the income approach converts future amounts, such as cash flows or earnings, to a single present amount, or a discounted amount. We believe the market approach valuation technique provides more observable data than the income approach, considering the types of investments we hold.

The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of pricing observability. Financial instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices in active markets generally have more pricing observability and less judgment utilized in measuring fair value. The market sources from which we obtain or derive the fair values of our assets and liabilities carried at market value include quoted market prices for actual trades, price quotes from third party pricing vendors, price quotes we obtain from outside brokers, matrix pricing, discounted cash flow, and observable prices for similar publicly traded or privately traded issues that incorporate the credit quality and industry sector of the issuer. Our fair value measurements could differ significantly based on the valuation technique and available inputs.

Inputs to valuation techniques refer broadly to the assumptions that market participants use in pricing assets or liabilities, including assumptions about risk, for example, the risk inherent in a particular valuation technique used to measure fair value and/or the risk inherent in the inputs to the valuation technique. We use observable and unobservable inputs in measuring the fair value of our financial instruments. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources. Unobservable inputs are inputs that reflect our own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

Certain of our investments do not have readily determinable market prices and/or observable inputs or may at times be affected by the lack of market liquidity. For these securities, we use internally prepared valuations combining matrix pricing with vendor purchased software programs, including valuations based on estimates of future profitability, to estimate the fair value. Additionally, we may obtain prices from independent third-party brokers to aid in establishing valuations for certain of these securities. Key assumptions used by us to determine fair value for these securities include risk free interest rates, risk premiums, performance of underlying collateral (if any), and other factors involving significant assumptions which may or may not reflect those of an active market.

As of December 31, 2014, the key assumptions we generally used to estimate the fair value of these types of securities included those listed below. Where appropriate, we have noted the assumption used for the prior period as well as the reason for the change.

- Risk free interest rates of 1.65 percent for five-year maturities to 2.75 percent for 30-year maturities were derived from the December 31, 2014 yield curve for U.S. Treasury Bonds with similar maturities. This compares to interest rates of 1.74 percent for five-year maturities to 3.97 percent for 30-year maturities used at December 31, 2013.
- Baa corporate bond spread adjustments ranging from 1.21 percent to 2.54 percent were added to the risk free rate to reflect additional credit risk and the lack of liquidity. We used spread adjustments ranging from 1.01 percent to 2.10 percent at December 31, 2013. The changes were based on observable market spreads. Newly issued private placement securities have historically offered yield premiums higher than a similar interest rate spread on comparable newly issued public securities.
- Additional basis points were added as deemed appropriate for foreign investments, certain industries, and individual securities in certain industries that are considered to be of greater risk.

As of December 31, 2014, approximately 6.6 percent of our fixed maturity securities were categorized as Level 1, 89.0 percent as Level 2, and 4.4 percent as Level 3. Level 1 is the highest category of the three-level fair value hierarchy classification wherein inputs are unadjusted and represent quoted prices in active markets for identical assets or liabilities. The Level 2 category includes assets or liabilities valued using inputs (other than those included in the Level 1 category) that are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life. The Level 3 category is the lowest category of the fair value hierarchy and reflects the judgment of management regarding what market participants would use in pricing assets or liabilities at the measurement date using unobservable inputs to extrapolate

an estimated fair value.

Rapidly changing credit and equity market conditions can materially impact the valuation of securities, and the period to period changes in value can vary significantly.

See Note 2 of the "Notes to Consolidated Financial Statements" contained herein in Item 8.

Investment Impairments

One of the significant estimates related to investments is our impairment valuation. In determining when a decline in fair value below amortized cost of a fixed maturity security is other than temporary, we evaluate the following factors:

- Whether we expect to recover the entire amortized cost basis of the security
- Whether we intend to sell the security or will be required to sell the security before the recovery of its amortized cost basis
- Whether the security is current as to principal and interest payments
- The significance of the decline in value
- The time period during which there has been a significant decline in value
- Current and future business prospects and trends of earnings
- The valuation of the security's underlying collateral
- Relevant industry conditions and trends relative to their historical cycles
- Market conditions
- Rating agency and governmental actions
- Bid and offering prices and the level of trading activity
- Adverse changes in estimated cash flows for securitized investments
- Changes in fair value subsequent to the balance sheet date
- Any other key measures for the related security

We evaluate available information, including the factors noted above, both positive and negative, in reaching our conclusions. In particular, we also consider the strength of the issuer's balance sheet, its debt obligations and near term funding requirements, cash flow and liquidity, the profitability of its core businesses, the availability of marketable assets which could be sold to increase liquidity, its industry fundamentals and regulatory environment, and its access to capital markets. Although all available and applicable factors are considered in our analysis, our expectation of recovering the entire amortized cost basis of the security, whether we intend to sell the security, whether it is more likely than not we will be required to sell the security before recovery of its amortized cost, and whether the security is current on principal and interest payments are the most critical factors in determining whether impairments are other than temporary. The significance of the decline in value and the length of time during which there has been a significant decline are also important factors, but we generally do not record an impairment loss based solely on these two factors, since often other more relevant factors will impact our evaluation of a security.

While determining other-than-temporary impairments is a judgmental area, we utilize a formal, well-defined, and disciplined process to monitor and evaluate our fixed income investment portfolio, supported by issuer specific research and documentation as of the end of each period. The process results in a thorough evaluation of problem investments and the recording of losses on a timely basis for investments determined to have an other-than-temporary impairment.

We use a comprehensive rating system to evaluate the investment and credit risk of our mortgage loans and to identify specific properties for inspection and reevaluation. Mortgage loans are considered impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. We establish an allowance for probable losses on mortgage loans based on a review of individual loans, considering the value of the underlying collateral, the value of which is periodically assessed. Mortgage loans are not reported at fair value in our consolidated balance sheets unless the mortgage loan is considered impaired, in which case the impairment is recognized as a realized investment loss in our consolidated statements of income.

45

There are a number of significant risks inherent in the process of monitoring our investments for impairments and determining when and if an impairment is other than temporary. These risks and uncertainties include the following possibilities:

- The assessment of a borrower's ability to meet its contractual obligations will change.
- The economic outlook, either domestic or foreign, may be less favorable or may have a more significant impact on the borrower than anticipated, and as such, the investment may not recover in value.
- New information may become available concerning the security, such as disclosure of accounting irregularities, fraud, or corporate governance issues.
- Significant changes in credit spreads may occur in the related industry.
- Significant increases in interest rates may occur and may not return to levels similar to when securities were initially purchased.
- Adverse rating agency actions may occur.

See Notes 1 and 3 of the "Notes to Consolidated Financial Statements" contained herein in Item 8.

Pension and Postretirement Benefit Plans

We sponsor several defined benefit pension and other postretirement benefit (OPEB) plans for our employees, including non-qualified pension plans. The U.S. qualified and non-qualified defined benefit pension plans comprise the majority of our total benefit obligation and benefit cost. We have a separate defined benefit plan for eligible employees in our U.K. operation.

During 2013, our U.S. defined benefit pension plans were closed to new entrants and were amended to freeze participation and benefit accruals as of December 31, 2013. In 2014, we further amended our U.S. qualified defined benefit pension plan to allow a limited-time offer of benefit payouts to eligible former employees with a vested right to a pension benefit. The offer provided eligible former employees, regardless of age, with an option to elect to receive a lump-sum settlement of his or her entire accrued pension benefit in December 2014 or to elect receipt of monthly pension benefits commencing in January 2015. For those who elected to receive lump-sum settlements, distributions from plan assets were made on or before December 31, 2014.

The U.K. defined benefit pension plan was closed to new entrants effective December 31, 2002 and was amended in 2013 to freeze participation effective June 30, 2014 and to reduce the maximum rate of inflation indexation from 5.0 percent to 2.5 percent for pension benefits which were earned prior to April 1997 effective at the date of adoption in 2013.

Assumptions

Our net periodic benefit costs and the value of our benefit obligations for these plans are determined based on a set of economic and demographic assumptions that represent our best estimate of future expected experience. Major assumptions used in accounting for these plans include the expected discount (interest) rate, the long-term rate of return on plan assets, and mortality rates. We also use, as applicable, expected increases in compensation levels and a weighted average annual rate of increase in the per capita cost of covered benefits, which reflects a health care cost trend rate, and the U.K. pension plan also uses expected cost of living increases to plan benefits.

The assumptions chosen for our pension and OPEB plans are reviewed annually, using a December 31 measurement date for each of our plans unless we are required to perform an interim remeasurement. The discount rate, expected long-term rate of return, and mortality rate assumptions have the most significant effect on our net periodic benefit costs associated with these plans. In addition to the effect of changes in our assumptions, the net periodic cost or

benefit obligation under our pension and OPEB plans may change due to factors such as plan amendments, actual experience being different from our assumptions, special benefits to terminated employees, and/or changes in benefits provided under the plans.

- Discount rate - This interest assumption is based on the yield derived from a portfolio of high quality fixed income corporate debt instruments that reasonably match the timing and amounts of projected future benefits for each of our retirement-related benefit plans. The rate is determined at the measurement date. A lower discount rate increases the present value of benefit obligations and increases our net periodic benefit cost.

- Long-term rate of return - This assumption is our best estimate of the average annual assumed return on plan assets until current benefits are paid. The market-related value as it relates to our estimate of long-term rate of return equals the fair value of plan assets, determined as of the measurement date. The return on plan assets recognizes all asset gains and losses, including changes in fair value, through the measurement date. Our expectations for the future

investment returns of the asset categories are based on a combination of historical market performance, evaluations of investment forecasts obtained from external consultants and economists, and current market yields. The expected return for the total portfolio is calculated based on the plan's current asset holdings. The actual rate of return on plan assets is determined based on the fair value of the plan assets at the beginning and the end of the period, adjusted for contributions and benefit payments. A lower long-term rate of return on plan assets increases our net periodic benefit cost.

Investment risk is measured and monitored on an ongoing basis through annual liability measurements, periodic asset/liability studies, and quarterly investment portfolio reviews. Risk tolerance is established through consideration of plan liabilities, plan funded status, and corporate financial condition. We believe our investment portfolios are well diversified by asset class and sector, with no potential risk concentrations in any one category. See Note 9 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of the investment portfolios for our plans.

- Mortality rate - This assumption reflects our best estimate, as of the measurement date, of the life expectancies of plan participants in order to determine the expected length of time for benefit payments. We derive our assumptions from industry mortality tables. The Society of Actuaries released updated mortality tables during the fourth quarter of 2014 which show that longevity in the United States is increasing, thereby establishing a new benchmark for mortality rates of private pension plan participants in the United States. Our mortality assumptions, which reflect the updated mortality tables, increased the benefit obligation of our U.S. defined benefit pension plans by approximately $125 million and of our OPEB plan by approximately $14 million. These updated tables do not impact the calculation of the benefit obligation for our U.K. defined benefit pension plan.

The weighted average assumptions used in the measurement of our net periodic benefit costs for the years ended December 31 are as follows:

	Pension Benefits					
	U.S. Plans		U.K. Plan		OPEB	
Assumption	2015	2014	2015	2014	2015	2014
Discount Rate	4.40 %	5.30 %	3.60 %	4.40 %	4.30 %	5.00 %
Expected Long-term Rate of Return on Plan Assets	7.50 %	7.50 %	5.20 %	6.10 %	5.75 %	5.75 %

The following illustrates the sensitivity of the below items to a 50 basis point change in the discount rate or the expected long-term rate of return on plan assets:

($ in millions)	At or for the Year Ended December 31, 2014			
Assumption	Change	Net Periodic Benefit Cost, Before Tax	Benefit Obligation	Stockholders' Equity, After Tax
Discount Rate	+ 50 bp	$(3.5)	$(181.9)	$121.4
Discount Rate	- 50 bp	2.6	205.9	(137.5)
Expected Long-term Rate of Return on Plan Assets	+ 50 bp	(9.1)	N/A	N/A
Expected Long-term Rate of Return on Plan Assets	- 50 bp	9.1	N/A	N/A

Benefit Obligation and Fair Value of Plan Assets

During 2014, the fair value of plan assets in our U.S. qualified defined benefit pension plan decreased $117.0 million, or approximately 7.4 percent, due primarily to the payment of $214.5 million in benefit payments related to our limited-time offer for benefit payouts, offset partially by an appreciation in the fair value of the remaining plan assets. The fair value of plan assets in our U.K. pension plan increased £21.7 million, or approximately 15.9 percent.

Although the effect of these changes in fair value had no impact on our 2014 net periodic pension costs, the favorable rate of return on these U.S. plan assets during 2014, in excess of our assumed rate of return for 2014, will have a favorable impact on our net periodic pension costs for 2015. This favorable impact on costs is offset by a decrease in the discount rate for all of our plans and a decrease in the expected long-term rate of return assumption for our U.K. pension plan assets. We believe our assumptions appropriately reflect the impact of the current economic environment.

Our pension and OPEB plans have an aggregate unrecognized net actuarial loss of $631.0 million and an unrecognized prior service credit of $0.7 million, which together represent the cumulative liability and asset gains and losses as well as the portion of prior service credits that have not been recognized in pension expense. As of December 31, 2014, the unrecognized net loss for these two items combined was $630.3 million.

The unrecognized gains or losses are amortized as a component of the net benefit cost. Our 2014, 2013, and 2012 pension and OPEB expense includes $3.9 million, $27.9 million, and $43.4 million, respectively, of amortization of the unrecognized net actuarial loss and prior service credit. Our 2014 net periodic benefit cost for our U.S. qualified defined benefit pension plan also includes a $64.4 million settlement loss related to our 2014 plan amendment, with a corresponding reduction in the unrecognized net actuarial loss in accumulated other comprehensive income. The unrecognized net actuarial loss for our pension plans, which is $628.4 million at December 31, 2014, will be amortized over the average remaining life expectancy of the plan participants, which is approximately 35 years for U.S. participants and 34 years for U.K. participants, to the extent that it exceeds the 10 percent corridor, as described below. The unrecognized net actuarial loss of $2.6 million for our OPEB plan will be amortized over the average future working life of OPEB plan participants, estimated at five years, to the extent the loss is outside of a corridor established in accordance with GAAP. The corridor for the pension and OPEB plans is established based on the greater of 10 percent of the plan assets or 10 percent of the benefit obligation. At December 31, 2014, $403.7 million of the actuarial loss was outside of the corridor for the U.S. plans and £6.9 million was outside of the corridor for the U.K. plan. At December 31, 2014, none of the actuarial loss was outside of the corridor for the OPEB plan.

The fair value of plan assets in our U.S. qualified defined benefit pension plan was $1,473.7 million at December 31, 2014, compared to $1,590.7 million at December 31, 2013. The plan was in a $245.1 million underfunded position at December 31, 2014 compared to an overfunded position of $13.4 million at December 31, 2013. This year-over-year change was due primarily to the decrease in the discount rate and the adoption of updated mortality assumptions.

The fair value of plan assets in our U.K. pension plan was £158.1 million at December 31, 2014, compared to £136.4 million at December 31, 2013. The U.K. pension plan was in an overfunded position of £12.4 million and £10.3 million at December 31, 2014 and 2013, respectively.

The fair value of plan assets in our OPEB plan was $11.3 million at December 31, 2014, compared to $11.4 million at December 31, 2013. These assets represent life insurance contracts to fund the life insurance benefit portion of our OPEB plan. Our OPEB plan represents a non-vested, non-guaranteed obligation, and current regulations do not require specific funding levels for these benefits, which are comprised of retiree life, medical, and dental benefits. It is our practice to use general assets to pay medical and dental claims as they come due in lieu of utilizing plan assets for the medical and dental benefit portions of our OPEB plan.

See Executive Summary contained herein in Item 7 and Note 9 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of our plans.

Income Taxes

We record a valuation allowance to reduce deferred tax assets to the amount that is more likely than not to be realized. In evaluating the ability to recover deferred tax assets, we have considered all available positive and negative evidence including past operating results, the existence of cumulative losses in the most recent years, forecasted earnings, future taxable income, and prudent and feasible tax planning strategies. In the event we determine that we most likely would not be able to realize all or part of our deferred tax assets in the future, an increase to the valuation allowance would be charged to earnings in the period such determination is made. Likewise, if it is later determined that it is more likely than not that those deferred tax assets would be realized, the previously provided valuation allowance would be reversed. As of December 31, 2014 and 2013, we had no valuation allowance.

The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax laws in a multitude of jurisdictions, both domestic and foreign. The amount of income taxes we pay is subject to ongoing audits in various jurisdictions, and a material assessment by a governing tax authority could affect profitability.

GAAP prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in income tax returns. The evaluation of a tax position is a two step process. The first step is to determine whether it is more likely than not that a tax position will be sustained upon examination based on the technical merits of the position. The second step is to measure a position that satisfies the recognition threshold at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more likely than not threshold but that now satisfy the recognition threshold are recognized in the first

subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more likely than not recognition threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met. If a previously recognized tax position is settled for an amount that is different from the amount initially measured, the difference will be recognized as a tax benefit or expense in the period the settlement is effective.

See Note 7 of the "Notes to Consolidated Financial Statements" contained herein in Item 8.

Contingent Liabilities

On a quarterly basis, we review relevant information with respect to litigation and contingencies to be reflected in our consolidated financial statements. An estimated loss is accrued when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. It is possible that our results of operations or cash flows in a particular period could be materially affected by an ultimate unfavorable outcome of pending litigation or regulatory matters depending, in part, on our results of operations or cash flows for the particular period. See Note 14 of the "Notes to Consolidated Financial Statements" contained herein in Item 8.

Accounting Developments

For information on new accounting standards and the impact, if any, on our financial position or results of operations, see Note 1 of the "Notes to Consolidated Financial Statements" contained herein in Item 8.

Consolidated Operating Results
(in millions of dollars)

	Year Ended December 31				
	2014	% Change	2013	% Change	2012
Revenue					
Premium Income	$7,797.2	2.3 %	$7,624.7	(1.2)%	$7,716.1
Net Investment Income	2,477.4	(0.6)	2,492.1	(0.9)	2,515.2
Net Realized Investment Gain	16.1	136.8	6.8	(87.9)	56.2
Other Income	219.0	(4.9)	230.2	1.0	227.9
Total Revenue	10,509.7	1.5	10,353.8	(1.5)	10,515.4
Benefits and Expenses					
Benefits and Change in Reserves for Future Benefits	7,310.8	10.8	6,595.7	(1.9)	6,722.2
Commissions	935.3	2.8	909.5	(0.8)	917.2
Interest and Debt Expense	167.5	12.1	149.4	2.8	145.4
Deferral of Acquisition Costs	(524.0)	12.3	(466.8)	(0.1)	(467.3)
Amortization of Deferred Acquisition Costs	440.8	5.2	418.9	10.6	378.7
Compensation Expense	820.9	3.9	790.4	0.5	786.8
Other Expenses	831.2	10.6	751.5	(4.0)	782.9
Total Benefits and Expenses	9,982.5	9.1	9,148.6	(1.3)	9,265.9
Income Before Income Tax	527.2	(56.3)	1,205.2	(3.5)	1,249.5
Income Tax	113.8	(67.2)	347.1	(2.3)	355.1
Net Income	$413.4	(51.8)	$858.1	(4.1)	$894.4

In describing our results, we may at times note certain items and exclude the impact on financial ratios and metrics to enhance the understanding and comparability of our operational performance and the underlying fundamentals, but this exclusion is not an indication that similar items may not recur. See "Reconciliation of Non-GAAP Financial Measures" contained in this Item 7 for additional discussion of these items.

The comparability of our financial results between years is affected by the fluctuation in the British pound sterling to dollar exchange rate. The functional currency of our U.K. operations is the British pound sterling. In periods when the pound weakens relative to the preceding period, translating pounds into dollars decreases current period results relative to the prior period. In periods when the pound strengthens, translating pounds into dollars increases current period results relative to the prior period. Our weighted average pound/dollar exchange rate was 1.646, 1.566, and 1.584 for years ended 2014, 2013, and 2012, respectively. If the 2013 and 2012 results for our U.K. operations had been translated at the higher exchange rate of 2014, our operating revenue by segment in 2013 and 2012 would have been higher by approximately $37.0 million and $32.9 million, respectively, and our operating income in 2013 and 2012 would have been higher by approximately $6.7 million and $5.1 million, respectively. However, it is important to distinguish between translating and converting foreign currency. Except for a limited number of transactions, we do not actually convert pounds into dollars. As a result, we view foreign currency translation as a financial reporting item and not a reflection of operations or profitability in the U.K.

Premium income for 2014 increased relative to the prior year, with premium growth in each of our principal operating business segments due to increased sales, premium rate increases, and favorable persistency in most of our product lines. While we are pleased with the improvement we saw throughout 2014, our premium growth rates remain below our long-term expectations for each of our principal operating business segments. For 2013, we reported premium

growth in our Unum US and Colonial Life segments relative to 2012, but premium income in total declined for 2013, as we believe growth in many of our product lines was unfavorably impacted during 2013 by the weak pace of economic growth, low levels of employment growth, the competitive environment, and the distraction caused by political instability and the implementation of healthcare reform. Also unfavorably impacting year over year comparisons for 2013 relative to 2012 were the reinsurance agreements we entered into during 2013 to cede a portion of certain product lines in Unum US individual disability and in Unum UK group life. Premium income continues to decline year over year, as expected, in our Closed Block segment.

Net investment income declined in 2014 relative to 2013 due primarily to a decrease in yield on invested assets and lower miscellaneous income, which includes income from bond call premiums, mortgage fees and payoffs, and partnership investments, partially offset by an increase in the level of invested assets. Net investment income was lower in 2013 relative to 2012 due primarily to a decline in the yield on invested assets, partially offset by a higher level of invested assets.

We recognized net realized investment gains of $16.1 million, $6.8 million, and $56.2 million in 2014, 2013, and 2012, respectively. The net realized investment gain for 2014 includes a $13.1 million hedge gain associated with the early retirement of a portion of the outstanding debt issued by one of our U.K. subsidiaries and an other-than-temporary impairment loss on fixed maturity securities of $13.5 million. The 2013 net realized investment gain includes a $30.0 million loss related to the sale of lower yielding securities during a period when interest rates increased, and we advantageously reinvested the proceeds into higher yielding investments, thereby increasing our investment yield and also improving the credit quality of our fixed maturity securities portfolio. Also included in net realized investment gains is the change in the fair value of an embedded derivative in a modified coinsurance arrangement, which resulted in realized gains of $3.3 million, $30.7 million, and $51.8 million in 2014, 2013, and 2012, respectively. See Notes 4 and 8 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of the hedge gain related to the retirement of debt in 2014.

The consolidated benefit ratios were 93.8 percent in 2014 compared to 86.5 percent in 2013 and 87.1 percent in 2012. Excluding the 2014 and 2013 reserve adjustments, the benefit ratios for 2014 and 2013 were 84.8 percent and 86.4 percent, respectively. The underlying risk results in 2014 for each of our principal operating business segments, as well as for the majority of our product lines within those segments, were favorable or consistent with the prior year periods.

Interest and debt expense for 2014 was higher than the prior year due primarily to the first quarter of 2014 issuance of $350 million of 4.00% senior notes, partially offset by the second quarter of 2014 retirement of $145 million of principal outstanding on 6.85% debt. Interest and debt expense for 2014 also includes $13.2 million of costs related to the second quarter of 2014 early retirement of debt. Interest and debt expense for 2013 was higher than 2012 due primarily to the issuance of $250 million of 5.75% senior notes in the third quarter of 2012, offset partially by lower interest expense on our floating rate debt and the purchase and retirement of the debt held by Tailwind Holdings, LLC (Tailwind Holdings) in the first quarter of 2013. See Note 8 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of our debt.

The deferral of acquisition costs increased in 2014 due primarily to sales growth in each of our principal operating business segments. The deferral of acquisition costs in 2013 was generally consistent with 2012. Amortization of acquisition costs was higher year-over-year in both 2014 and 2013 due to growth in the level of the deferred assets in our Unum US and Colonial Life businesses. Also contributing to the increase in amortization of acquisition costs in 2013 compared to 2012 was a higher level of policy terminations experienced in 2013 relative to assumptions for certain issue years within some of our Unum US supplemental and voluntary product lines.

Other expenses, including compensation expense, increased in 2014 compared to 2013 due to an increase in acquisition-related expenses, including sales compensation, resulting from higher sales in certain of our product lines, higher expenses related to technology and other growth-related investments, increased contributions to our defined contribution plans as a result of amendments to these plans which became effective in 2014, and the settlement loss related to our 2014 pension plan amendment. Partially offsetting these expense increases is a lower level of net actuarial loss amortization in 2014 compared to 2013 due to pension plan amendments adopted during 2013. Other expenses, including compensation expense, were in aggregate lower in 2013 relative to 2012 due to active expense management, the impact of the mid-year 2013 pension plan amendments, and expense reductions associated with reinsurance agreements entered into during 2013. See Note 9 in the "Notes to Consolidated Financial Statements"

contained herein in Item 8 for further discussion of our employee benefit plans.

Our income tax for 2014 was 21.6 percent of income before income tax, compared to 28.8 percent and 28.4 percent in 2013 and 2012, respectively. Our effective tax rate differs from the U.S. statutory rate of 35 percent primarily due to tax credits for tax credit partnerships and foreign earnings taxed at lower rates than the U.S. statutory rate. Our overall rate for 2014 was favorably impacted because a larger proportion of our 2014 earnings was derived from our foreign operations and taxed at that lower rate due to the long-term care reserve charge which is taxed at the higher U.S. rate. Our income tax for 2013 and 2012 includes reductions of $6.3 million and $9.3 million, respectively, to reflect the impact of the decrease in the U.K. corporation tax rate changes on our net deferred tax liability related to our U.K. operations. Our 2012 income tax also includes a release of an $11.0 million tax liability related to unrecognized tax benefits. See Note 7 in the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further information on our income tax.

Further discussion of operating results for each of our segments and major product lines is included in "Segment Operating Results" herein in Item 7.

Consolidated Sales Results

Shown below are sales results for our three principal operating business segments.
(in millions)

	Year Ended December 31							
	2014	% Change		2013	% Change		2012
Unum US	$902.1	21.0	%	$745.6	(2.0	)%	$760.5
Unum UK	£51.9	7.2	%	£48.4	(18.7	)%	£59.5
Colonial Life	$410.1	11.6	%	$367.6	1.6	%	$361.9

Sales shown in the preceding chart generally represent the annualized premium income on new sales which we expect to receive and report as premium income during the next 12 months following or beginning in the initial quarter in which the sale is reported, depending on the effective date of the new sale. Sales do not correspond to premium income reported as revenue in accordance with GAAP. This is because new annualized sales premiums reflect current sales performance and what we expect to recognize as premium income over a 12 month period, while premium income reported in our financial statements is reported on an "as earned" basis rather than an annualized basis and also includes renewals and persistency of in-force policies written in prior years as well as current new sales.
Sales, persistency of the existing block of business, employment and salary growth, and the effectiveness of a renewal program are indicators of growth in premium income. Trends in new sales, as well as existing market share, also indicate the potential for growth in our respective markets and the level of market acceptance of price changes and new product offerings. Sales results may fluctuate significantly due to case size and timing of sales submissions.
See "Segment Results" as follows for a discussion of sales by segment.

Segment Results

Our reporting segments are comprised of the following: Unum US, Unum UK, Colonial Life, Closed Block, and Corporate. Financial information for each of our reporting segments is as follows.

Unum US Segment

The Unum US segment includes group long-term and short-term disability insurance, group life and accidental death and dismemberment products, and supplemental and voluntary lines of business, which are comprised of individual disability and voluntary benefits products.

Unum US Operating Results

Shown below are financial results for the Unum US segment. In the sections following, financial results and key ratios are also presented for the major lines of business within the segment.
(in millions of dollars, except ratios)

	Year Ended December 31								
	2014		% Change		2013		% Change		2012
Operating Revenue									
Premium Income	$4,659.7		3.2	%	$4,517.1		1.4	%	$4,456.5
Net Investment Income	890.3		(4.2	)	929.6		(2.4	)	952.3
Other Income	122.1		(4.8	)	128.3		3.0		124.6
Total	5,672.1		1.7		5,575.0		0.8		5,533.4
Benefits and Expenses									
Benefits and Change in Reserves for Future Benefits	3,288.1		2.0		3,222.4		(0.5	)	3,238.6
Commissions	528.7		4.7		505.2		(0.5	)	507.5
Deferral of Acquisition Costs	(292.7	)	16.2		(252.0	)	1.1		(249.2	)
Amortization of Deferred Acquisition Costs	248.1		7.9		230.0		17.0		196.5
Other Expenses	1,043.6		4.3		1,000.8		0.8		992.9
Total	4,815.8		2.3		4,706.4		0.4		4,686.3
Income Before Income Tax and Net Realized Investment Gains and Losses	856.3		(1.4	)	868.6		2.5		847.1
Unclaimed Death Benefits (UDB) Reserve Increase	—		—		75.4		—		—
Group Life Waiver of Premium Benefit (Waiver) Reserve Reduction	—		—		(85.0	)	—		—
Operating Income	$856.3		(0.3	)	$859.0		1.4		$847.1
Operating Ratios (% of Premium Income):									
Benefit Ratio	70.6	%			71.3	%			72.7	%
Benefit Ratio Excluding the UDB and Waiver Reserve Adjustments					71.6	%			
Other Expense Ratio	22.4	%			22.2	%			22.3	%
Income Ratio	18.4	%			19.2	%			19.0	%
Operating Income Ratio	18.4	%			19.0	%			19.0	%

53

Unum US Group Disability Operating Results

Shown below are financial results and key performance indicators for Unum US group disability.

(in millions of dollars, except ratios)

	Year Ended December 31				
	2014	% Change	2013	% Change	2012
Operating Revenue					
Premium Income					
Group Long-term Disability	$1,553.5	— %	$1,553.9	(1.6)%	$1,578.8
Group Short-term Disability	558.1	7.4	519.6	9.0	476.7
Total Premium Income	2,111.6	1.8	2,073.5	0.9	2,055.5
Net Investment Income	519.1	(5.6)	550.1	(4.6)	576.9
Other Income	91.0	(4.8)	95.6	2.0	93.7
Total	2,721.7	0.1	2,719.2	(0.3)	2,726.1
Benefits and Expenses					
Benefits and Change in Reserves for Future Benefits	1,746.4	0.8	1,732.9	(0.5)	1,741.6
Commissions	161.2	(1.7)	164.0	3.0	159.3
Deferral of Acquisition Costs	(40.2)	35.8	(29.6)	12.5	(26.3)
Amortization of Deferred Acquisition Costs	26.3	24.6	21.1	15.3	18.3
Other Expenses	550.0	3.3	532.4	(1.4)	540.1
Total	2,443.7	0.9	2,420.8	(0.5)	2,433.0
Operating Income	$278.0	(6.8)	$298.4	1.8	$293.1
Operating Ratios (% of Premium Income):					
Benefit Ratio	82.7 %		83.6 %		84.7 %
Other Expense Ratio	26.0 %		25.7 %		26.3 %
Operating Income Ratio	13.2 %		14.4 %		14.3 %
Persistency:					
Group Long-term Disability	90.6 %		87.2 %		90.7 %
Group Short-term Disability	89.6 %		88.0 %		88.0 %

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Premium income increased in 2014 compared to 2013, driven by favorable persistency, premium rate increases, and sales growth for both group long-term and group short-term disability. Net investment income declined in 2014 relative to 2013 due to a decrease in the level of invested assets and a decline in yield. Other income is comprised primarily of fees from administrative services products, which declined slightly in 2014 relative to 2013. Also included in other income for 2013 is a gain of $4.0 million on the purchase and retirement of the debt issued by Tailwind Holdings.

Risk results were favorable in 2014 compared to 2013 due primarily to favorable claim recovery experience, partially offset by slightly higher claim incidence rates and a 50 basis point decrease in the discount rate which we implemented during the fourth quarter of 2014 for group long-term disability new claim incurrals.

The deferral of acquisition costs was higher in 2014 relative to the prior year due to an increase in deferrable expenses related to sales growth. The amortization of acquisition costs increased in 2014 compared to 2013 due to growth in the

level of the deferred asset. The other expense ratio for 2014 was higher compared to 2013 due to an increase in other expenses driven by technology and other growth-related investments, a higher level of allocated retirement-related costs, and higher acquisition-related expenses resulting from the increased level of sales.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Premium income increased slightly in 2013 compared to 2012 primarily due to growth from rate increases, partially offset by a decline in persistency in the group long-term disability product line. We believe the weak pace of economic growth, low levels of employment growth, and competitive environment hampered our premium income growth in 2013, including growth from existing customers. Net investment income declined in 2013 relative to 2012 due to decreases in the level of invested assets, lower miscellaneous income, and a decrease in the yield on invested assets. Other income increased slightly in 2013 compared to 2012 due to the gain of $4.0 million on the purchase and retirement of the debt issued by Tailwind Holdings, partially offset by a decrease in fees from administrative services products.

Risk results were favorable in 2013 compared to 2012 due to favorable claim incidence rates and continued strong claim recovery experience. These results were partially offset by the 50 basis point decrease in the discount rate which we implemented during the third quarter of 2012 for group long-term disability new claim incurrals.

The deferral and amortization of acquisition costs were both higher in 2013 relative to 2012 due to an increase in deferrable expenses and the resulting continued growth in the level of the deferred asset. The other expense ratio for 2013 was lower compared to 2012 as we continued to focus on operating effectiveness and expense management relative to our premium income level.

Unum US Group Life and Accidental Death and Dismemberment Operating Results

Shown below are financial results and key performance indicators for Unum US group life and accidental death and dismemberment.

(in millions of dollars, except ratios)

	Year Ended December 31								
	2014		% Change		2013		% Change		2012
Operating Revenue									
Premium Income									
Group Life	$1,262.3		4.0	%	$1,213.9		2.7	%	$1,182.1
Accidental Death & Dismemberment	125.9		3.5		121.6		5.5		115.3
Total Premium Income	1,388.2		3.9		1,335.5		2.9		1,297.4
Net Investment Income	139.2		(2.4	)	142.6		(2.9	)	146.9
Other Income	1.4		(22.2	)	1.8		(5.3	)	1.9
Total	1,528.8		3.3		1,479.9		2.3		1,446.2
Benefits and Expenses									
Benefits and Change in Reserves for Future Benefits	975.8		7.2		909.9		(2.8	)	936.4
Commissions	113.3		4.0		108.9		4.1		104.6
Deferral of Acquisition Costs	(31.3	)	26.7		(24.7	)	10.3		(22.4	)
Amortization of Deferred Acquisition Costs	21.4		37.2		15.6		14.7		13.6
Other Expenses	205.2		3.5		198.2		2.6		193.1
Total	1,284.4		6.3		1,207.9		(1.4	)	1,225.3
Income Before Income Tax and Net Realized Investment Gains and Losses	244.4		(10.1	)	272.0		23.1		220.9
Unclaimed Death Benefits (UDB) Reserve Increase	—		—		49.1		—		—
Group Life Waiver of Premium Benefit (Waiver) Reserve Reduction	—		—		(85.0	)	—		—
Operating Income	$244.4		3.5		$236.1		6.9		$220.9
Operating Ratios (% of Premium Income):									
Benefit Ratio	70.3	%			68.1	%			72.2	%
Benefit Ratio Excluding the UDB and Waiver Reserve Adjustments					70.8	%			
Other Expense Ratio	14.8	%			14.8	%			14.9	%
Income Ratio	17.6	%			20.4	%			17.0	%
Operating Income Ratio	17.6	%			17.7	%			17.0	%
Persistency:									
Group Life	90.8	%			88.1	%			90.6	%
Accidental Death & Dismemberment	91.1	%			88.8	%			90.0	%

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Premium income increased in 2014 compared to 2013 primarily due to continued growth in the block of business resulting from sales and favorable persistency. Net investment income was lower in 2014 relative to the prior year due to a decrease in the yield on invested assets and lower miscellaneous income, partially offset by an increase in the

level of invested assets.

Risk results were unfavorable in 2014 compared to the prior year due to the net favorable impact of the 2013 reserve adjustments for group life waiver of premium benefits and unclaimed death benefits. Excluding these two reserve adjustments, risk results were slightly favorable in 2014 compared to 2013 due to lower claim incidence rates, partially offset by a higher average claim size.

The deferral of acquisition costs was higher in 2014 relative to the prior year due to sales growth. The amortization of acquisition costs increased in 2014 compared to 2013 due to growth in the level of the deferred asset. The other expense ratio in 2014 was consistent with the prior year as the increase in premium income more than offset expense increases driven by technology and other growth-related investments, a higher level of allocated retirement-related costs, and higher acquisition-related expenses resulting from the increased level of sales.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Premium income increased in 2013 compared to 2012 primarily due to growth in the block of business which resulted from sales and premium rate increases, partially offset by a decline in persistency. Net investment income was lower in 2013 compared to 2012 primarily due to a decrease in the yield on invested assets, partially offset by an increase in the level of invested assets.

Risk results were favorable in 2013 compared to 2012 as a result of the 2013 reserve reduction for group life waiver of premium benefits, partially offset by the reserve increase for unclaimed death benefits. Excluding these two reserve adjustments, risk results were favorable in 2013 compared to 2012 due primarily to more favorable experience related to the group life waiver of premium benefits.

The deferral and amortization of acquisition costs were both higher in 2013 relative to the prior year due to an increase in deferrable expenses and the resulting continued growth in the level of the deferred asset. The other expense ratio in 2013 was consistent with 2012.

Unum US Supplemental and Voluntary Operating Results

Shown below are financial results and key performance indicators for Unum US supplemental and voluntary product lines.

(in millions of dollars, except ratios)

	Year Ended December 31								
	2014		% Change		2013		% Change		2012
Operating Revenue									
Premium Income									
Individual Disability	$466.1		0.2	%	$465.3		(2.6	)%	$477.6
Voluntary Benefits	693.8		7.9		642.8		2.7		626.0
Total Premium Income	1,159.9		4.7		1,108.1		0.4		1,103.6
Net Investment Income	232.0		(2.1	)	236.9		3.7		228.5
Other Income	29.7		(3.9	)	30.9		6.6		29.0
Total	1,421.6		3.3		1,375.9		1.1		1,361.1
Benefits and Expenses									
Benefits and Change in Reserves for Future Benefits	565.9		(2.4	)	579.6		3.4		560.6
Commissions	254.2		9.4		232.3		(4.6	)	243.6
Deferral of Acquisition Costs	(221.2	)	11.9		(197.7	)	(1.4	)	(200.5	)
Amortization of Deferred Acquisition Costs	200.4		3.7		193.3		17.4		164.6
Other Expenses	288.4		6.7		270.2		4.0		259.7
Total	1,087.7		0.9		1,077.7		4.8		1,028.0
Income Before Income Tax and Net Realized Investment Gains and Losses	333.9		12.0		298.2		(10.5	)	333.1
Unclaimed Death Benefits (UDB) Reserve Increase	—		—		26.3		—		—
Operating Income	$333.9		2.9		$324.5		(2.6	)	$333.1
Interest Adjusted Loss Ratio:									
Individual Disability	30.0	%			29.6	%			31.2	%
Operating Ratios (% of Premium Income):									
Benefit Ratios:									
Individual Disability	51.6	%			51.3	%			52.4	%
Voluntary Benefits	46.9	%			53.0	%			49.5	%
Benefit Ratio Excluding the UDB Reserve Increase									
Voluntary Benefits					48.9	%			
Other Expense Ratio	24.9	%			24.4	%			23.5	%
Income Ratio	28.8	%			26.9	%			30.2	%
Operating Income Ratio	28.8	%			29.3	%			30.2	%
Persistency:									
Individual Disability	90.0	%			90.5	%			91.4	%
Voluntary Benefits	77.6	%			77.0	%			78.9	%

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Premium income was higher in 2014 compared to 2013, driven primarily by higher sales and stable to favorable persistency. Net investment income was lower in 2014 relative to 2013 due to decrease in yield on invested assets and lower miscellaneous income, partially offset by an increase in the level of invested assets.

Risk results for the individual disability product line were slightly less favorable during 2014 compared to 2013 due to lower claim recoveries and higher claim incidence rates. Risk results for voluntary benefits were favorable compared to 2013 due to the 2013 reserve increase for unclaimed death benefits. Excluding this reserve increase, risk results were favorable due to improved claim experience in the disability and life product lines.

Commissions and deferral of acquisition costs were higher in 2014 relative to 2013 due primarily to higher sales. The amortization of deferred acquisition costs was higher in 2014 compared to the prior year due to growth in the level of the deferred asset. The other expense ratio for 2014 increased compared to 2013 due to an increase in other expenses driven by technology and other growth-related investments, a higher level of allocated retirement-related costs, and higher acquisition-related expenses resulting from the increased level of sales.

The individual disability product line had goodwill of approximately $187.5 million at December 31, 2014, none of which is currently believed to be at risk for future impairment.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Premium income was generally consistent in 2013 compared to 2012, with growth in voluntary benefits offset by a decrease in the individual disability product line due to a reinsurance contract entered into during the second quarter of 2013 to cede a small block of individual disability business. Persistency for both individual disability and voluntary benefits declined relative to 2012 due to a higher level of policy terminations in the early part of 2013. Net investment income was higher in 2013 compared to 2012 due to an increase in the level of invested assets, an increase in miscellaneous income, partially offset by a decline in the yield on invested assets.

Risk results for the individual disability product line were favorable during 2013 compared to 2012 due to higher claim recoveries and the impact of a release of active life reserves related to the termination of a large in-force policy in 2013. Risk results for voluntary benefits were unfavorable compared to 2012 as a result of the 2013 reserve increase for unclaimed death benefits. Excluding this reserve increase, risk results for voluntary benefits were slightly favorable in 2013 compared to 2012 due to favorable experience in the life and critical illness product lines.

Commissions were lower in 2013 relative to 2012 due primarily to amounts ceded under the individual disability reinsurance contract previously discussed. The deferral of acquisition costs was generally consistent in 2013 compared to 2012. The amortization of deferred acquisition costs was higher in 2013 compared to 2012 due to a less favorable year-over-year impact from the prospective unlocking for expected future experience relative to assumptions for our interest-sensitive voluntary life products as well as a higher level of policy terminations relative to assumptions for certain issue years within certain of our product lines. The other expense ratio in 2013 was higher than 2012 due primarily to lower premium income resulting from the reinsurance contract entered into during 2013 in our individual disability product line as well as higher expenses associated with our voluntary benefits products.

Sales
(in millions of dollars)

	Year Ended December 31						
	2014	% Change		2013	% Change		2012
Sales by Product							
Group Disability and Group Life and AD&D							
Group Long-term Disability	$223.6	29.0	%	$173.3	(4.9	)%	$182.2
Group Short-term Disability	118.8	16.6		101.9	4.6		97.4
Group Life and AD&D	264.8	32.8		199.4	(3.9	)	207.5
Subtotal	607.2	27.9		474.6	(2.6	)	487.1
Supplemental and Voluntary							
Individual Disability	56.8	8.8		52.2	(8.4	)	57.0
Voluntary Benefits	238.1	8.8		218.8	1.1		216.4
Subtotal	294.9	8.8		271.0	(0.9	)	273.4
Total Sales	$902.1	21.0		$745.6	(2.0	)	$760.5
Sales by Market Sector							
Group Disability and Group Life and AD&D							
Core Market (< 2,000 lives)	$401.7	23.8	%	$324.4	(3.1	)%	$334.9
Large Case Market	205.5	36.8		150.2	(1.3	)	152.2
Subtotal	607.2	27.9		474.6	(2.6	)	487.1
Supplemental and Voluntary	294.9	8.8		271.0	(0.9	)	273.4
Total Sales	$902.1	21.0		$745.6	(2.0	)	$760.5

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Sales of our group products increased in 2014 relative to 2013 in both the core and large case market segments for new and existing customer accounts. The sales mix in the group market sector for 2014 was approximately 66 percent core market and 34 percent large case market, generally consistent with the level of 2013.

Sales in our individual disability line of business, which are primarily concentrated in the multi-life market, increased in 2014 due to a favorable mix of sales in the core and large case market segments. Sales of voluntary benefits were higher in 2014 compared to 2013, with increases in both core and large case market sales.

We attribute a portion of our 2014 sales growth relative to 2013 to the distraction which occurred in the marketplace during 2013 as a result of healthcare reform implementation, which we believe negatively impacted our core market sales for our group and voluntary benefits products throughout 2013.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Sales in our group core and large case market segments declined in 2013 relative to 2012. In both markets, sales to existing accounts increased in 2013 but this increase was more than offset by a decrease in new account sales. The decline in new sales in our group core market was driven by fewer sales opportunities in the small-size employer market segment during 2013, which we believe may have been temporarily attributable to healthcare reform as well as the uncertain economic and political environment. We believe the decline in new sales in our large case market was partially due to our disciplined and opportunistic approach to sales growth. The sales mix in our group market sector in 2013 was approximately 68 percent core market and 32 percent large case market, generally consistent with the prior year.

Sales in our individual disability line of business were lower in 2013 compared to 2012 due to lower sales growth from existing customers. Sales of voluntary benefits were higher in 2013 compared to 2012, with an increase in core market sales partially offset by a decrease in large case market sales.

Segment Outlook

During 2015, we expect continued strong growth momentum, with continued strong persistency and sales growth within our existing client relationships. We believe we will achieve year-over-year growth in premium income, with additional improvement in our premium and sales growth rates if the overall economic recovery further accelerates and market pricing adequately reflects the impact of a low interest rate environment.

Our net investment income may be impacted, either favorably or unfavorably, by fluctuations in miscellaneous investment income. The low interest rate environment and tighter credit spreads continue to place pressure on our profit margins by impacting net investment income yields and claim reserve discount rates. As part of our continued pricing discipline and our reserving strategy, we continuously monitor emerging interest rate experience and adjust our pricing and reserve discount rates, as appropriate. We expect a stable risk environment for our group disability product line in 2015, with the impact of the lower claim reserve discount rate offset by premium rate increases we place in the market, resulting in a benefit ratio for full year 2015 that is generally consistent with the level of 2014.

Our amortization of deferred acquisition costs may be unfavorably impacted, particularly in our supplemental and voluntary product line, by higher than expected policy terminations. We believe future profit margin improvement is achievable, driven primarily by our continued product mix shift, expense efficiencies, and consistent operating effectiveness.

Certain risks and uncertainties are inherent in the disability insurance business. Components of claims experience, such as incidence and recovery rates, may be worse than we expect. Disability claim incidence and claim recovery rates may be influenced by, among other factors, the rate of unemployment and consumer confidence. Within the group disability market, pricing and renewal actions can be taken to react to higher claim rates or lower discount rates, but these actions take time to implement, and there is a risk that the market will not sustain increased prices. In addition, changes in economic and external conditions may not manifest themselves in claims experience for an extended period of time. Unfavorable economic conditions may lead to a higher rate of claim incidence, lower levels of claim recoveries, or lower claim discount rates. Claim incidence levels may fluctuate due to the normal volatility that occurs in group disability business or may be related to economic conditions. We continuously monitor key indicators to assess our risks and attempt to adjust our business plans accordingly.

We remain confident in our strategy of providing consumers with valuable financial protection benefits, broadening our employer client relationships, and building collaborative partnerships with complementary product manufacturers, technology firms, and distributors. Our continued investment in our franchise includes active client management and a differentiated integrated experience across our product lines. There are significant growth opportunities in each of our markets and within our existing client base, and we continue to invest in the people, processes, and technologies that will allow us to enhance our ability to grow the market over the long term. Underpinning our strategy is our continued commitment to risk management discipline, talent development, and our core values.

Unum UK Segment

The Unum UK segment includes insurance for group long-term disability, group life, and supplemental lines of business which include individual disability and critical illness. Unum UK's products are sold primarily in the United Kingdom through field sales personnel and independent brokers and consultants.

Operating Results

Shown below are financial results and key performance indicators for the Unum UK segment.

(in millions of dollars, except ratios)

	Year Ended December 31				
	2014	% Change	2013	% Change	2012
Operating Revenue					
Premium Income					
Group Long-term Disability	$418.9	7.4 %	$389.9	(4.8)%	$409.7
Group Life	133.2	25.2	106.4	(51.9)	221.3
Supplemental	55.1	(8.6)	60.3	(5.2)	63.6
Total Premium Income	607.2	9.1	556.6	(19.9)	694.6
Net Investment Income	151.0	1.7	148.5	(13.1)	170.8
Other Income	—	(100.0)	0.1	—	0.1
Total	758.2	7.5	705.2	(18.5)	865.5
Benefits and Expenses					
Benefits and Change in Reserves for Future Benefits	431.0	4.3	413.3	(23.7)	541.4
Commissions	42.8	12.6	38.0	(10.8)	42.6
Deferral of Acquisition Costs	(10.5)	7.1	(9.8)	(16.9)	(11.8)
Amortization of Deferred Acquisition Costs	12.5	(15.0)	14.7	(6.4)	15.7
Other Expenses	134.6	15.0	117.0	(20.0)	146.3
Total	610.4	6.5	573.2	(21.9)	734.2
Operating Income	$147.8	12.0	$132.0	0.5	$131.3
Operating Ratios (% of Premium Income):					
Benefit Ratio	71.0 %		74.3 %		77.9 %
Other Expense Ratio	22.2 %		21.0 %		21.1 %
Operating Income Ratio	24.3 %		23.7 %		18.9 %
Persistency:					
Group Long-term Disability	90.1 %		82.2 %		84.0 %
Group Life	76.0 %		66.7 %		82.5 %
Supplemental	86.6 %		78.8 %		84.6 %

Foreign Currency Translation

The functional currency of Unum UK is the British pound sterling. Unum UK's premium income, net investment income, claims, and expenses are received or paid in pounds, and we hold pound-denominated assets to support Unum UK's pound-denominated policy reserves and liabilities. We translate Unum UK's pound-denominated financial statement items into dollars for our consolidated financial reporting. We translate income statement items using an average exchange rate for the reporting period, and we translate balance sheet items using the exchange rate at the end of the period. We report unrealized foreign currency translation gains and losses in accumulated other comprehensive income in our consolidated balance sheets.

Fluctuations in the pound to dollar exchange rate have an effect on Unum UK's reported financial results and our consolidated financial results. In periods when the pound strengthens relative to the preceding period, translating pounds into dollars increases current period results relative to the prior period. In periods when the pound weakens, translating pounds into dollars decreases current period results relative to the prior period.

(in millions of pounds, except ratios)

	Year Ended December 31				
	2014	% Change	2013	% Change	2012
Operating Revenue					
Premium Income					
Group Long-term Disability	£254.4	2.1 %	£249.2	(3.6)%	£258.4
Group Life	80.8	18.5	68.2	(51.1)	139.6
Supplemental	33.4	(13.2)	38.5	(4.0)	40.1
Total Premium Income	368.6	3.6	355.9	(18.8)	438.1
Net Investment Income	91.6	(3.5)	94.9	(11.9)	107.7
Other Income	0.1	—	0.1	—	—
Total	460.3	2.1	450.9	(17.4)	545.8
Benefits and Expenses					
Benefits and Change in Reserves for Future Benefits	261.4	(1.2)	264.5	(22.5)	341.4
Commissions	26.0	7.0	24.3	(9.7)	26.9
Deferral of Acquisition Costs	(6.4)	3.2	(6.2)	(17.3)	(7.5)
Amortization of Deferred Acquisition Costs	7.6	(18.3)	9.3	(6.1)	9.9
Other Expenses	81.9	9.6	74.7	(19.0)	92.2
Total	370.5	1.1	366.6	(20.8)	462.9
Operating Income	£89.8	6.5	£84.3	1.7	£82.9
Weighted Average Pound/Dollar Exchange Rate	1.646		1.566		1.584

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Premium income was higher in 2014 compared to 2013 due to premium rate increases in our group long-term disability and group life product lines, favorable persistency, and an increased retention level in our reinsurance program, as of January 1, 2014, for our group life products that provide lump sum benefits. Partially offsetting these increases were large case policy terminations in our group life and supplemental product lines.

Net investment income declined in 2014 compared to 2013 due primarily to lower yields on invested assets. We also reported lower income from inflation index-linked bonds which we invest in to support the claim reserves associated

with certain of our group policies that provide for inflation-linked increases in benefits.

Group long-term disability and group life risk results were favorable in 2014 compared to 2013 due primarily to lower claim incidence rates. Supplemental risk results were favorable in 2014 compared to 2013 due to lower claim incidence rates for the group critical illness product line.

Commissions were higher in 2014 compared to 2013 due primarily to the increased retention level in our group life reinsurance program. The amortization of deferred acquisition costs was lower in 2014 compared to the prior year due primarily to a decrease in the level of the deferred asset. The other expense ratio was higher in 2014 compared to the prior year due primarily to an increase in operational investments in our business and a lower comparative expense ratio in 2013 as a result of expense allowances related to the reinsurance agreements in our group life product line.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Premium income was lower in 2013 compared to 2012 due primarily to reinsurance agreements we entered into effective January 1, 2013 to cede an additional portion of our group life business. The reinsurance agreements significantly decreased premium income and benefit payments for group life during 2013 and also reduced volatility in this line of business. Premium income in 2013 was also unfavorably impacted by continued pressure on persistency resulting from the initiation of premium rate increases, partially offset by an increase in premium income as a result of rate increases in existing customer accounts.

Net investment income declined in 2013 compared to 2012 due primarily to a decrease in the yield on invested assets, lower levels of invested assets, and lower income from inflation index-linked bonds.

Group long-term disability risk results were unfavorable in 2013 compared to 2012 due primarily to lower claim recoveries. Group life risk results were favorable in 2013 compared to 2012 due primarily to lower mortality rates on the retained business. Supplemental risk results were favorable in 2013 compared to the prior year due to lower claim incidence rates for the group critical illness product line.

Commissions and deferral of acquisition costs were lower in 2013 compared to 2012 due to expenses ceded under the group life reinsurance agreements and a lower level of sales in 2013. The amortization of deferred acquisition costs and the other expense ratio were generally consistent in 2013 compared to the prior year.

Sales
(in millions of dollars and pounds)

	Year Ended December 31						
	2014	% Change		2013	% Change		2012
Sales by Product							
Group Long-term Disability	$57.4	13.7	%	$50.5	(1.4	)%	$51.2
Group Life	23.8	11.2		21.4	(43.7	)	38.0
Supplemental	3.9	—		3.9	(20.4	)	4.9
Total Sales	$85.1	12.3		$75.8	(19.4	)	$94.1
Sales by Market Sector							
Group Long-term Disability and Group Life							
Core Market (< 500 lives)	$42.5	9.3	%	$38.9	0.5	%	$38.7
Large Case Market	38.7	17.3		33.0	(34.7	)	50.5
Subtotal	81.2	12.9		71.9	(19.4	)	89.2
Supplemental	3.9	—		3.9	(20.4	)	4.9
Total Sales	$85.1	12.3		$75.8	(19.4	)	$94.1
Sales by Product							
Group Long-term Disability	£35.1	9.0	%	£32.2	(0.3	)%	£32.3
Group Life	14.4	5.1		13.7	(43.2	)	24.1
Supplemental	2.4	(4.0	)	2.5	(19.4	)	3.1
Total Sales	£51.9	7.2		£48.4	(18.7	)	£59.5
Sales by Market Sector							
Group Long-term Disability and Group Life							
Core Market (< 500 lives)	£25.8	3.6	%	£24.9	2.0	%	£24.4
Large Case Market	23.7	12.9		21.0	(34.4	)	32.0
Subtotal	49.5	7.8		45.9	(18.6	)	56.4
Supplemental	2.4	(4.0	)	2.5	(19.4	)	3.1
Total Sales	£51.9	7.2		£48.4	(18.7	)	£59.5

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Sales in group long-term disability increased in 2014 compared to 2013 due to higher sales in the large case market, with an increase in sales to new customers partially offset by lower sales to existing customers. In the group long-term disability core market, or employee groups with fewer than 500 lives, sales declined in 2014 relative to the prior year.

Group life sales within the core market segment were higher in 2014 compared to 2013 for both new and existing customers. Group life sales in the large case market declined in 2014 relative to the prior year due to decreased sales to existing customers, partially offset by higher sales to new customers.

Supplemental sales were lower in 2014 compared to 2013 due primarily to lower sales in our group critical illness product line.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Sales in group long-term disability in 2013 were consistent with 2012, with higher new account sales and an increase in core market sales offset by a decrease in sales to existing customers and a decline in sales in the large case market.

Group life sales were lower in 2013 compared to 2012 as a result of declines in new account sales in both the core and large case markets, which more than offset higher sales to existing customers. The decrease in group life sales was due in part to pricing discipline and the initiation of rate increases on new business. Also impacting the comparability of group life sales relative to 2012 was the discontinuance of new sales of certain of our group life product lines beginning in the third quarter of 2012.

Supplemental sales were lower in 2013 compared to 2012 due primarily to lower sales in our individual disability product line.

Segment Outlook

Our primary focus during 2015 will be a continuance of building on the key capabilities that we believe will enable us to deliver future growth. We expect to continue to improve our profitability through our shift in business mix, premium rate increases, an increased focus on new to market sales, and continued pursuit of efficiency opportunities.

We expect the low interest rate environment to continue to contribute to a dampening of overall earnings growth, and unfavorable economic conditions may lead to a higher rate of claim incidence, lower levels of claim recoveries, or lower claim discount rates. We are also preparing for Solvency II, a new European Union capital regime that will become effective January 1, 2016, the adoption of which will likely result in an increase in supervisory and disclosure requirements and could also result in increased capital requirements. We continue to work with regulatory authorities in the U.K. to agree on appropriate capital requirements for our U.K. business under Solvency II. We continuously monitor key indicators to assess our risks and attempt to adjust our business plans accordingly.

In our group life business, the completion of our near-term actions regarding rate increases, reinsurance, and the discontinuance of certain product lines have reduced volatility and contributed to improvement in our overall profit margin. We are now looking at opportunities for disciplined growth in this market segment.

In our group long-term disability business, we remain committed to driving growth in the U.K. market. We will continue to follow a disciplined approach to new sales activity in the competitive pricing environment. We do, however, see genuine opportunities to grow the group long-term disability market in the U.K. through establishing new relationships with employers, deepening the level of coverage with our existing corporate clients, and through new offerings such as a sick-pay product and an updated offering of our group critical illness product. We anticipate returning to more normal levels of premium growth as our rate increases continue to be placed in the market and as we continue to increase sales to new and existing customers. We have seen some positive results in terms of new to market sales and increased coverage in existing cases. We believe the outlook for higher levels of employment, increases in corporate payrolls, and expansion of benefit spending is beginning to improve and will positively impact our sales and operating results, but a sustained low interest rate environment may dampen our profitability. In addition, we continue to focus on new market opportunities by raising awareness of the need for income protection. Expanding group long-term disability market penetration remains a significant opportunity and priority.

Colonial Life Segment

The Colonial Life segment includes insurance for accident, sickness, and disability products, life products, and cancer and critical illness products issued primarily by Colonial Life & Accident Insurance Company and marketed to employees at the workplace through an independent contractor agency sales force and brokers.

Operating Results

Shown below are financial results and key performance indicators for the Colonial Life segment.

(in millions of dollars, except ratios)

	Year Ended December 31				
	2014	% Change	2013	% Change	2012
Operating Revenue					
Premium Income					
Accident, Sickness, and Disability	$759.8	2.9 %	$738.7	2.0 %	$724.5
Life	231.8	4.8	221.1	5.4	209.7
Cancer and Critical Illness	282.1	3.6	272.4	4.6	260.3
Total Premium Income	1,273.7	3.4	1,232.2	3.2	1,194.5
Net Investment Income	146.7	0.9	145.4	4.9	138.6
Other Income	0.1	(50.0)	0.2	(33.3)	0.3
Total	1,420.5	3.1	1,377.8	3.3	1,333.4
Benefits and Expenses					
Benefits and Change in Reserves for Future Benefits	660.6	(1.0)	667.0	6.3	627.3
Commissions	262.3	3.9	252.5	(0.8)	254.5
Deferral of Acquisition Costs	(220.8)	7.7	(205.0)	(0.6)	(206.3)
Amortization of Deferred Acquisition Costs	180.2	3.4	174.2	4.6	166.5
Other Expenses	238.0	6.1	224.3	3.3	217.1
Total	1,120.3	0.7	1,113.0	5.1	1,059.1
Income Before Income Tax and Net Realized Investment Gains and Losses	300.2	13.4	264.8	(3.5)	274.3
Unclaimed Death Benefits (UDB) Reserve Increase	—	—	20.1	—	—
Operating Income	$300.2	5.4	$284.9	3.9	$274.3
Operating Ratios (% of Premium Income):					
Benefit Ratio	51.9 %		54.1 %		52.5 %
Benefit Ratio Excluding the UDB Reserve Increase			52.5 %		
Other Expense Ratio	18.7 %		18.2 %		18.2 %
Income Ratio	23.6 %		21.5 %		23.0 %
Operating Income Ratio	23.6 %		23.1 %		23.0 %
Persistency:					
Accident, Sickness, and Disability	75.5 %		75.2 %		75.7 %
Life	85.2 %		85.2 %		85.7 %
Cancer and Critical Illness	83.5 %		83.1 %		84.5 %

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Premium income increased in 2014 relative to 2013 due to sales and continued strong persistency. Net investment income was higher in 2014 relative to the prior year due to an increase in the level of invested assets, partially offset by a decrease in yield on invested assets and lower miscellaneous income.

Favorable risk results in 2014 compared to 2013 primarily reflect improved claim experience in the cancer and critical illness product line. This was partially offset by less favorable experience in the accident, sickness, and disability product line due to a higher average claim size and in the life product line due to less favorable mortality experience. The release of active life reserves on terminations of older cases in the accident, sickness, and disability and cancer and critical illness product lines also favorably impacted 2014 relative to 2013.

Commissions and the deferral of acquisition costs were higher in 2014 relative to 2013 due to sales growth. The amortization of deferred acquisition costs was higher in 2014 compared to the prior year due primarily to continued growth in the level of the deferred asset. The other expense ratio was higher in 2014 compared to 2013 due primarily to continued investment in our business, higher sales compensation, and a higher level of allocated retirement-related costs.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Premium income increased in 2013 relative to 2012 due to continued growth in the block of business as a result of sales and continued strong persistency. Net investment income increased in 2013 due to an increase in the level of invested assets and higher miscellaneous income, partially offset by a decrease in the yield on invested assets.

Our reported risk results for 2013 were less favorable than in 2012 as a result of the reserve increase for unclaimed death benefits. Excluding this reserve increase, the benefit ratio of 52.5 percent was consistent with the level of 2012, with favorable risk results in the life product line, due to improved mortality experience, offsetting less favorable risk results in the accident, sickness, and disability and cancer and critical illness product lines that resulted from an increased level of incurred claims.

Commissions and the deferral of acquisition costs were generally consistent in 2013 compared to 2012. The amortization of deferred acquisition costs was higher in 2013 compared to 2012 due to continued growth in the level of the deferred asset as well as higher amortization resulting from the prospective unlocking for expected future experience relative to assumptions for our interest-sensitive life products. The increase in other expenses in 2013 compared to 2012 was commensurate with the growth in premium income.

Sales
(in millions of dollars)

	Year Ended December 31						
	2014	% Change		2013	% Change		2012
Sales by Product							
Accident, Sickness, and Disability	$260.7	9.4	%	$238.2	2.2	%	$233.0
Life	78.8	15.7		68.1	1.2		67.3
Cancer and Critical Illness	70.6	15.2		61.3	(0.5)		61.6
Total Sales	$410.1	11.6		$367.6	1.6		$361.9
Sales by Market Sector							
Commercial							
Core Market (< 1,000 lives)	$275.6	12.0	%	$246.0	(0.9)	%	$248.3
Large Case Market	53.2	8.6		49.0	19.8		40.9
Subtotal	328.8	11.5		295.0	2.0		289.2
Public Sector	81.3	12.0		72.6	(0.1)		72.7
Total Sales	$410.1	11.6		$367.6	1.6		$361.9

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Sales were higher in 2014 compared to 2013 due to growth in both new and existing customer account sales and across all market segments. Commercial market sales increased in 2014, with higher sales in both the core commercial market, which we define as accounts with fewer than 1,000 lives, and in the large case commercial market. The growth in our core commercial market sales for 2014 was primarily attributable to new account sales, although we also experienced favorable growth in existing account sales. The growth in the large case commercial market was primarily attributable to higher sales to existing accounts. Public sector sales for 2014 increased due primarily to new account sales. The number of new accounts increased 13.4 percent in 2014 compared to 2013, and the average new case size increased 5.8 percent.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Sales were slightly higher in 2013 than 2012, with growth in existing account sales in all market segments. This growth was partially offset by a slight decrease in new account sales, with the decline primarily occurring in the core commercial market. Although large case commercial market sales were significantly higher than 2012, our new business pricing was within our guidelines as we continued our disciplined yet opportunistic approach to sales growth in this market. We believe the 2013 decrease in core commercial market sales, particularly in the small employer segment, was partially attributable to healthcare reform as well as the uncertain economic and political environment. The number of new accounts decreased 18.2 percent in 2013 compared to 2012, while the average new case size increased 20.0 percent.

Segment Outlook

We expect to see continued favorable sales and premium growth trends in 2015. Volatility in net investment income is likely to continue as a result of fluctuations in miscellaneous investment income. We expect our annual benefit ratio for 2015 to be generally consistent with the level of 2014. While we expect the low interest rate environment to continue to pressure our profit margins, we believe our underlying profitability will remain strong.

Proper execution of our growth strategy should deliver sales and premium growth that are in line with long-term expectations. Unfavorable U.S. economic conditions and the increasing competition in the voluntary market are seen as external risks to achievement of our business plans. We continuously monitor key indicators to assess our risks and attempt to adjust our business plans accordingly.

We believe our success will be driven primarily by execution in the core commercial and public sector segments and through expansion of the overall market. We believe the current market environment offers considerable opportunities to meet the emerging needs of employers, brokers, and consumers. We intend to continue to focus on growth, the customer experience, productivity, and talent development. Achieving our 2015 growth objectives will be supported by a continued focus on third-party connectivity, enrollment solutions, service capabilities, and operational excellence.

Closed Block Segment

The Closed Block segment consists of individual disability, group and individual long-term care, and other insurance products no longer actively marketed. The individual disability line of business in this segment generally consists of policies we sold prior to the mid-1990s and entirely discontinued selling in 2004, other than update features contractually allowable on existing policies. We discontinued offering individual long-term care in 2009 and group long-term care in 2012. Other insurance products include group pension, individual life and corporate-owned life insurance, reinsurance pools and management operations, and other miscellaneous product lines.

Operating Results

Shown below are financial results and key performance indicators for the Closed Block segment.
(in millions of dollars, except ratios)

	Year Ended December 31					
	2014	% Change	2013	% Change	2012	
Operating Revenue						
Premium Income						
Individual Disability	$624.8	(9.1)%	$687.5	(6.6)%	$736.4	
Long-term Care	630.9	—	630.6	(0.2)	631.9	
All Other	0.9	28.6	0.7	(68.2)	2.2	
Total Premium Income	1,256.6	(4.7)	1,318.8	(3.8)	1,370.5	
Net Investment Income	1,284.1	0.9	1,272.3	3.4	1,230.5	
Other Income	91.8	(2.2)	93.9	(6.2)	100.1	
Total	2,632.5	(2.0)	2,685.0	(0.6)	2,701.1	
Benefits and Expenses						
Benefits and Change in Reserves for Future Benefits	2,931.1	27.8	2,293.0	(0.9)	2,314.9	
Commissions	101.5	(10.8)	113.8	1.1	112.6	
Interest and Debt Expense	7.3	(13.1)	8.4	(19.2)	10.4	
Other Expenses	168.2	4.9	160.4	(4.4)	167.7	
Total	3,208.1	24.6	2,575.6	(1.2)	2,605.6	
Income (Loss) Before Income Tax and Net Realized Investment Gains and Losses	(575.6)	(626.1)	109.4	14.6	95.5	
Long-term Care Reserve Increase	698.2	—	—	—	—	
Operating Income	$122.6	12.1	$109.4	14.6	$95.5	
Interest Adjusted Loss Ratios:						
Individual Disability	83.6 %		82.6 %		83.0 %	
Long-term Care	196.6 %		89.6 %		90.1 %	
Long-term Care Excluding the Reserve Increase	85.9 %					
Operating Ratios (% of Premium Income):						
Other Expense Ratio	13.4 %		12.2 %		12.2 %	
Income (Loss) Ratio	(45.8)%		8.3 %		7.0 %	
Operating Income Ratio	9.8 %		8.3 %		7.0 %	

Persistency:

Individual Disability	91.3	%	91.8	%	92.5	%
Long-term Care	95.4	%	95.5	%	95.8	%

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Total premium income decreased in 2014 compared to 2013 due to expected policy terminations and maturities. The premium decrease resulting from persistency trends in the long-term care line of business was partially offset by the favorable impact of premium rate increases on certain of these policies. We continue to file requests with various state insurance departments for premium rate increases on certain of our individual and group long-term care policies. The rate increases reflect current interest rates and claim experience, higher expected future claims, longevity, persistency, and other factors related to pricing long-term care coverage. In states for which a rate increase is submitted and approved, customers are also given options for coverage changes or other approaches that might fit their current financial and insurance needs.

Net investment income was higher in 2014 relative to 2013 due to increased invested asset levels and higher miscellaneous income, partially offset by a decrease in yield on invested assets. Other income, which includes the underlying results of certain blocks of individual disability reinsured business and the net investment income of portfolios held by those ceding companies to support the block we have reinsured, was lower in 2014 compared to 2013 primarily due to lower investment income from the investment portfolios held by the ceding companies.

Individual disability risk results for 2014 were unfavorable relative to 2013 due primarily to higher claim incidence rates. Long-term care risk results were unfavorable in 2014 relative to the prior year due to the reserve charge, as previously discussed. Excluding this charge, long-term care risk results were favorable compared to 2013 due to lower claim incidence rates.

Commissions decreased in 2014 compared to 2013 due to a lower level of accrued commissions in 2014 as well as the expected run-off of these blocks of business. Interest and debt expense in 2014 was lower than 2013 due to principal repayments on the outstanding debt issued by Northwind Holdings, LLC (Northwind Holdings) and a decrease in the floating rate of interest. The other expense ratio was higher compared to 2013 due to lower premium income and an increase in expenses attributable to our long-term care product line.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Total premium income decreased in 2013 compared to 2012 due to expected policy terminations and maturities, partially offset by the favorable impact of premium rate increases on certain of our long-term care policies as well as the issuance of group long-term care certificates on in-force cases.

Net investment income was higher in 2013 compared to 2012 due primarily to higher invested asset levels, partially offset by a decrease in the yield on invested assets. Other income was lower in 2013 compared to 2012 due in part to lower investment income in the portfolios held by the ceding companies to which we have ceded certain blocks of individual disability business.

Individual disability risk results for 2013 were slightly favorable compared to 2012 due primarily to lower claim incidence rates. Long-term care risk results were slightly favorable in 2013 compared to 2012 due to more favorable development in active life reserves.

Interest and debt expense in 2013 was lower than 2012 due to principal repayments on the outstanding debt issued by Northwind Holdings and a decrease in the floating rate of interest. The other expense ratio was consistent in 2013 compared to 2012.

Segment Outlook

We intend to continue our focus on operational effectiveness, rate increases, enhancement of our experience analysis tools, and capital management. We expect operating revenue to decline over time as these closed blocks of business wind down, although we anticipate additional premium income associated with long-term care rate increases. We also expect a small amount of group long-term care certificates may continue to be issued where we are required to do so under the terms of existing group policies. We will likely experience volatility in net investment income due to fluctuations of miscellaneous investment income. We continuously monitor key indicators to assess our risks and attempt to adjust our business plans accordingly. We expect the low interest rate environment and the tightening of credit spreads to continue to place pressure on our earnings and reserve levels.

Profitability of our long-tailed products is affected by claims experience related to mortality and morbidity, investment returns, premium rate increases, and persistency. We believe that the interest adjusted loss ratios for the individual disability and long-term care lines of business will be relatively flat over the long term, but these product lines may continue to experience quarterly volatility, particularly in the near term for our long-term care product lines as our claim block matures. Claim resolution rates, which measure the resolution of claims from recovery, deaths, settlements, and benefit expirations, are very sensitive to operational and external factors and can be volatile. Our claim resolution rate assumption used in determining reserves is our expectation of the resolution rate we will experience over the life of the block of business and will vary from actual experience in any one period. It is possible that variability in any of our reserve assumptions, including, but not limited to, interest rates, mortality, morbidity, premium rate increases, and persistency, could result in a material impact on our reserve levels, including adjustments to reserves established under loss recognition.

Corporate Segment

The Corporate segment includes investment income on corporate assets not specifically allocated to a line of business, interest expense on corporate debt other than non-recourse debt, and certain other corporate income and expense not allocated to a line of business.

Operating Results
(in millions of dollars)

	Year Ended December 31				
	2014	% Change	2013	% Change	2012
Operating Revenue					
Net Investment Income	$5.3	N.M.	$(3.7)	N.M.	$23.0
Other Income	5.0	(35.1)	7.7	175.0	2.8
Total	10.3	157.5	4.0	(84.5)	25.8
Interest and Other Expenses	157.9	7.1	147.5	9.8	134.3
Operating Loss Including Costs Related to Early Retirement of Debt	(147.6)	(2.9)	(143.5)	(32.3)	(108.5)
Costs Related to Early Retirement of Debt	13.2	—	—	—	—
Operating Loss	$(134.4)	6.3	$(143.5)	(32.3)	$(108.5)

N.M. = not a meaningful percentage

Year Ended December 31, 2014 Compared with Year Ended December 31, 2013

Net investment income increased in 2014 relative to 2013 due to higher levels of invested assets, partially offset by a decrease in yield on invested assets. Also impacting the year over year comparison for all years presented is the negative impact on reported net investment income attributable to the amortization of tax credit partnerships, the amounts of which are generally offset in income tax expense by a lower income tax rate due to the tax benefits recognized as a result of these investments. An accounting guidance update which is effective January 1, 2015 permits us to account for tax credit partnerships using proportional amortization and allows us to recognize that amortization as a component of income tax expense rather than as negative net investment income. See Note 1 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for discussion of this update.

Other income declined in 2014 relative to the prior year due primarily to the recognition of income in 2013 related to a settlement of an appeal to the IRS for tax years 2005 to 2006.

Interest and other expenses were higher in 2014 compared to 2013 due to $13.2 million of costs related to the 2014 retirement of a portion of debt and due to increased interest expense on debt, partially offset by a higher level of retirement-related costs allocated from Corporate to our other segments.

Year Ended December 31, 2013 Compared with Year Ended December 31, 2012

Net investment income was lower in 2013 compared to 2012 due to a decrease in the yield on invested assets, a decrease in reported investment income attributable to tax credit partnerships, and lower short-term interest rates.

Other income was higher in 2013 compared to 2012 due primarily to the IRS settlement.

Interest and other expenses were higher in 2013 compared to 2012 due primarily to an increase in interest expense on debt and a higher level of expense accruals in 2013 relative to the prior year.

Segment Outlook

We are currently holding capital at our insurance subsidiaries and holding companies at levels that exceed our long-term requirements, and we expect to continue to generate excess capital on an annual basis through our statutory earnings. While we intend to maintain our disciplined approach to risk management, we believe we are well positioned with substantial flexibility to preserve our capital strength and at the same time explore opportunities to deploy the excess capital that is generated.

Investments
Overview

Our investment portfolio is well diversified by type of investment and industry sector. We have established an investment strategy that we believe will provide for adequate cash flows from operations and allow us to hold our securities through periods where significant decreases in fair value occur. We believe our emphasis on risk management in our investment portfolio, including credit and interest rate management, has positioned us well and generally reduced the volatility in our results.

Below is a summary of our formal investment policy, including the overall quality and diversification objectives:

- The majority of investments are in high quality publicly traded securities to ensure the desired liquidity and preserve the capital value of our portfolios.
- The long-term nature of our insurance liabilities also allows us to invest in less liquid investments to obtain superior returns. A maximum of 10 percent of the total investment portfolio may be invested in below-investment-grade securities, 2 percent in equity securities, 3 percent in tax credit partnerships, 35 percent in private placements, and 10 percent in commercial mortgage loans. The remaining assets can be held in publicly traded investment-grade corporate securities, mortgage/asset backed securities, bank loans, government and government agency securities, and municipal securities.
- We intend to manage the risk of losses due to changes in interest rates by matching asset duration with liabilities, in the aggregate.
- The weighted average credit quality rating of the portfolio should be Baa1 or higher.
- The maximum investment per issuer group is limited based on internal limits reviewed by the risk and finance committee of Unum Group's board of directors and approved by the boards of directors of our insurance subsidiaries and is more restrictive than the five percent limit generally allowed by the state insurance departments which regulate the type of investments our insurance subsidiaries are allowed to own. These internal limits are as follows:

Rating	Internal Limit ($ in millions)
AAA/AA	$200
A	175
BBB+	150
BBB	125
BBB-	90
BB+	75
BB	60
BB-	50
B+	30
B/B-	20
CCC	10

- The portfolio is to be diversified across industry classification and geographic lines.
- Derivative instruments may be used to replicate permitted asset classes, hedge interest rate risk, credit risk, and foreign currency risk, and match liability duration and cash flows consistent with the plan reviewed by the risk and finance committee of Unum Group's board of directors and approved by the boards of directors of our insurance subsidiaries.
- Asset mix guidelines and limits are established by us, reviewed by the risk and finance committee of Unum Group's board of directors, and approved by the boards of directors of our insurance subsidiaries.

- The allocation of assets and the selection and timing of the acquisition and disposition of investments are subject to ratification, on a weekly basis, by an investment subcommittee appointed by the boards of directors of our insurance subsidiaries. These actions are also reviewed by the risk and finance committee of Unum Group's board of directors on a quarterly basis.
- We review these investment policies and guidelines annually, or more frequently if deemed necessary, and recommend adjustments, as appropriate. Any revisions or exceptions are reviewed by the risk and finance committee of Unum Group's board of directors and must be approved by the boards of directors of our insurance subsidiaries.

See "Critical Accounting Estimates" contained in this Item 7 for further discussion of our valuation of investments.

Fixed Maturity Securities

The fair values and associated unrealized gains and losses of our fixed maturity securities portfolio, by industry classification, are as follows:

Fixed Maturity Securities - By Industry Classification
As of December 31, 2014
(in millions of dollars)

Classification	Fair Value	Net Unrealized Gain	Fair Value of Fixed Maturity Securities with Gross Unrealized Loss	Gross Unrealized Loss	Fair Value of Fixed Maturity Securities with Gross Unrealized Gain	Gross Unrealized Gain
Basic Industry	$2,666.8	$244.0	$366.4	$29.1	$2,300.4	$273.1
Capital Goods	3,946.5	523.0	113.8	4.1	3,832.7	527.1
Communications	3,110.4	502.5	106.4	3.0	3,004.0	505.5
Consumer Cyclical	1,284.9	172.6	24.7	0.4	1,260.2	173.0
Consumer Non-Cyclical	5,961.6	814.2	486.2	12.7	5,475.4	826.9
Energy	6,117.3	690.4	952.5	68.9	5,164.8	759.3
Financial Institutions	3,389.0	396.4	—	—	3,389.0	396.4
Mortgage/Asset-Backed	2,431.8	206.9	29.9	0.1	2,401.9	207.0
Sovereigns	1,307.4	206.3	—	—	1,307.4	206.3
Technology	1,211.8	93.5	282.1	3.6	929.7	97.1
Transportation	1,676.9	269.8	63.5	0.4	1,613.4	270.2
U.S. Government Agencies and Municipalities	3,360.0	631.5	51.0	1.6	3,309.0	633.1
Public Utilities	8,550.6	1,504.5	63.3	0.9	8,487.3	1,505.4
Redeemable Preferred Stocks	49.9	5.9	—	—	49.9	5.9
Total	$45,064.9	$6,261.5	$2,539.8	$124.8	$42,525.1	$6,386.3

Our investment portfolio has exposure to companies whose businesses are negatively impacted by lower oil and natural gas prices. These include exploration and production companies, refineries, midstream and pipeline companies, and oilfield service businesses. The recent sharp drop in the price of oil is putting pressure on the earnings and cash flows of some of these businesses. The midstream and pipeline subsector represents our largest exposure within the energy sector. Demand for products in this subsector tends to be more correlated to product volume sales as opposed to the commodity price. We have very little exposure to the oilfield service subsector where demand for products is highly correlated with oil and gas prices. The degree to which a business is affected by oil and gas prices

can vary greatly depending on, among other things, its energy subsector, exposure to different types of oil and gas within a subsector, geographic locations, cost structure flexibility, capital structure, and hedging policies. The majority of our energy sector holdings are investment-grade fixed maturity securities. We perform stress testing on all energy-related investments in our portfolios, using different oil and gas price scenarios, and we continue to closely monitor this situation. Currently, we expect downward ratings pressure on some of our securities, but we do not expect material losses in our energy sector investments.

The following two tables show the length of time our investment-grade and below-investment-grade fixed maturity securities had been in a gross unrealized loss position as of December 31, 2014 and at the end of the prior four quarters. The relationships of the current fair value to amortized cost are not necessarily indicative of the fair value to amortized cost relationships for the

securities throughout the entire time that the securities have been in an unrealized loss position nor are they necessarily indicative of the relationships after December 31, 2014. The decrease in the unrealized loss on investment-grade fixed maturity securities during 2014 was due primarily to a decrease in U.S. Treasury rates which occurred during the period. The increase in the unrealized loss on below-investment-grade fixed maturity securities during 2014 was due primarily to an increase in credit spreads in certain industries or sectors. We held no fixed maturity securities at December 31, 2014 with a gross unrealized loss of $10.0 million or greater.

Unrealized Loss on Investment-Grade Fixed Maturity Securities
Length of Time in Unrealized Loss Position
(in millions of dollars)

	2014				2013
	December 31	September 30	June 30	March 31	December 31
Fair Value < 100% >= 70% of Amortized Cost					
<= 90 days	$23.2	$10.1	$2.2	$4.6	$20.0
> 90 <= 180 days	0.7	0.2	—	0.3	11.5
> 180 <= 270 days	0.1	—	0.1	2.9	183.3
> 270 days <= 1 year	—	—	1.0	85.6	12.6
> 1 year <= 2 years	20.4	34.2	43.6	13.8	11.0
> 2 years <= 3 years	2.2	—	—	0.1	—
> 3 years	0.9	3.1	3.4	6.2	6.9
Sub-total	47.5	47.6	50.3	113.5	245.3
Fair Value < 70% >= 40% of Amortized Cost					
> 3 years	—	—	—	—	2.5
Total	$47.5	$47.6	$50.3	$113.5	$247.8

Unrealized Loss on Below-Investment-Grade Fixed Maturity Securities
Length of Time in Unrealized Loss Position
(in millions of dollars)

	2014				2013
	December 31	September 30	June 30	March 31	December 31
Fair Value < 100% >= 70% of Amortized Cost					
<= 90 days	$20.2	$20.8	$0.1	$1.2	$2.6
> 90 <= 180 days	31.4	0.4	—	0.7	2.5
> 180 <= 270 days	—	—	0.6	0.9	29.9
> 270 days <= 1 year	—	0.5	—	8.1	1.7
> 1 year <= 2 years	12.8	8.4	6.2	1.4	0.9
> 2 years <= 3 years	0.4	0.3	0.5	2.4	4.1
> 3 years	5.7	6.6	7.3	11.3	14.1
Sub-total	70.5	37.0	14.7	26.0	55.8
Fair Value < 70% >= 40% of Amortized Cost					

<= 90 days	6.8	—	—	—	—
> 3 years	—	—	—	0.3	0.3
Sub-total	6.8	—	—	0.3	0.3
Total	$77.3	$37.0	$14.7	$26.3	$56.1

During 2014, we recognized an other-than-temporary impairment loss of $13.5 million on fixed maturity securities issued by a U.S.-based oil and natural gas exploration and production company. The company has a high debt-to-equity ratio, and its projected liquidity has recently decreased significantly as a result of the declines in oil and natural gas prices. We believe the

company will need to sell non-core assets to maintain liquidity and to build and develop its core assets. This process will be more difficult if the low oil price environment persists for an extended period of time. At the time of the impairment loss, these securities had been in an unrealized loss position for a period of greater than 90 days but less than 180 days. We had no individual realized investment losses of $10.0 million or greater from other-than-temporary impairments during 2013 or 2012.

We had no individual realized investment losses of $10.0 million or greater from the sale of fixed maturity securities during 2014 or 2013. During 2012, we recognized a loss of $11.2 million on the sale of securities issued by a large U.S. department store chain. In 2011, the company's management was replaced by a new team of executives that embarked on a radically different retailing strategy. While the company had ample liquidity and sizable value in real estate assets, initial operating results under this new strategy had been significantly below market expectations, and there was uncertainty as to whether this new strategy would be successful. Because of this, we had concerns that liquidity could be compromised over an extended period of time. At the time of disposition, these securities had been in an unrealized loss position for a period of greater than three years.

At December 31, 2014, we had minimal exposure to investments for which the payment of interest and principal is guaranteed under a financial guaranty insurance policy, and the securities in aggregate have a weighted average credit rating of investment-grade absent the guaranty insurance policy. At December 31, 2014, we held $191.1 million fair value ($169.7 million amortized cost) of perpetual debentures, or "hybrid" securities, that generally have no fixed maturity date. Interest on these securities due on any payment date may be deferred by the issuer. The interest payments are generally deferrable only to the extent that the issuer has suspended dividends or other distributions or payments to any of its shareholders or any other perpetual debt instrument.

At December 31, 2014, our mortgage/asset-backed securities had an average life of 4.85 years, effective duration of 4.14 years, and a weighted average credit rating of Aaa. The mortgage/asset-backed securities are valued on a monthly basis using valuations supplied by the brokerage firms that are dealers in these securities as well as independent pricing services. One of the risks involved in investing in mortgage/asset-backed securities is the uncertainty of the timing of cash flows from the underlying loans due to prepayment of principal with the possibility of reinvesting the funds in a lower interest rate environment. We use models which incorporate economic variables and possible future interest rate scenarios to predict future prepayment rates. The timing of prepayment cash flows may also cause volatility in our recognition of investment income. We recognize investment income on these securities using a constant effective yield based on projected prepayments of the underlying loans and the estimated economic life of the securities. Actual prepayment experience is reviewed periodically, and effective yields are recalculated when differences arise between prepayments originally projected and the actual prepayments received and currently projected. The effective yield is recalculated on a retrospective basis, and the adjustment is reflected in net investment income.

We have no exposure to subprime mortgages, "Alt-A" loans, or collateralized debt obligations in our investment portfolios. We have not invested in mortgage-backed derivatives, such as interest-only, principal-only, or residuals, where market values can be highly volatile relative to changes in interest rates. The credit quality of our mortgage-backed securities portfolio has not been negatively impacted by the issues in the market concerning subprime mortgage loans. The change in value of our mortgage-backed securities portfolio has moved in line with that of prime agency-backed mortgage-backed securities.

As of December 31, 2014, the amortized cost and fair value of our below-investment-grade fixed maturity securities was $3,454.2 million and $3,525.2 million, respectively. Below-investment-grade securities are inherently more risky than investment-grade securities since the risk of default by the issuer, by definition and as exhibited by bond rating, is higher. Also, the secondary market for certain below-investment-grade issues can be highly illiquid. Additional downgrades may occur, but we do not anticipate any liquidity problems resulting from our investments in

below-investment-grade securities, nor do we expect these investments to adversely affect our ability to hold our other investments to maturity.

Our investments in issuers in foreign countries are chosen for specific portfolio management purposes, including asset and liability management and portfolio diversification across geographic lines and sectors to minimize non-market risks. In our approach to investing in fixed maturity securities, specific investments within approved countries and industry sectors are evaluated for their market position and specific strengths and potential weaknesses. For each security, we consider the political, legal, and financial environment of the sovereign entity in which an issuer is domiciled and operates. The country of domicile is based on consideration of the issuer's headquarters, in addition to location of the assets and the country in which the majority of sales and earnings are derived. We do not have exposure to foreign currency risk, as the cash flows from these investments are either denominated in currencies or hedged into currencies to match the related liabilities. We continually evaluate our foreign investment risk exposure. Our monitoring is heightened for investments in certain countries due to our concerns over the current economic and political environments as well as the banking crisis, and we believe these investments are more vulnerable to potential credit problems. At December 31, 2014, we had minimal exposure in those countries and had no direct exposure to financial institutions of those countries.

Mortgage Loans

Our mortgage loan portfolio was $1,856.6 million and $1,815.1 million on an amortized cost basis at December 31, 2014 and 2013, respectively. Our mortgage loan portfolio is comprised entirely of commercial mortgage loans. We believe our mortgage loan portfolio is well diversified geographically and among property types. The incidence of problem mortgage loans and foreclosure activity continues to be low. Due to conservative underwriting, we expect the level of problem loans to remain low relative to the industry.

We held one mortgage loan at December 31, 2014 and 2013 that was considered impaired and was carried at the estimated net realizable value of $13.1 million, net of a valuation allowance of $1.5 million.

Derivative Financial Instruments

We use derivative financial instruments primarily to manage reinvestment, duration, foreign currency, and credit risks. Historically, we have utilized current and forward interest rate swaps and options on forward interest rate swaps and U.S. Treasury rates, current and forward currency swaps, forward treasury locks, currency forward contracts, forward contracts on specific fixed income securities, and credit default swaps. Our current credit exposure on derivatives, which is limited to the value of those contracts in a net gain position, including accrued interest receivable less collateral held, was $13.6 million at December 31, 2014. We held $15.4 million of cash collateral from our counterparties at December 31, 2014. The carrying value of fixed maturity securities posted as collateral to our counterparties was $67.0 million at December 31, 2014. We had no cash collateral posted to our counterparties at December 31, 2014. We believe that our credit risk is mitigated by our use of multiple counterparties, all of which have a median credit rating of A3 or better, and by our use of cross-collateralization agreements.

Other

Our exposure to non-current investments, defined as foreclosed real estate and invested assets which are delinquent as to interest and/or principal payments, totaled $40.4 million and $39.9 million on a fair value basis at December 31, 2014 and 2013, respectively.

See Notes 3 and 4 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of our investments and our derivative financial instruments.

Liquidity and Capital Resources

Overview

Our liquidity requirements are met primarily by cash flows provided from operations, principally in our insurance subsidiaries. Premium and investment income, as well as maturities and sales of invested assets, provide the primary sources of cash. Debt and/or securities offerings provide additional sources of liquidity. Cash is applied to the payment of policy benefits, costs of acquiring new business (principally commissions), operating expenses, and taxes, as well as purchases of new investments.

We have established an investment strategy that we believe will provide for adequate cash flows from operations. We attempt to match our asset cash flows and durations with expected liability cash flows and durations to meet the funding requirements of our business. However, deterioration in the credit market may delay our ability to sell our positions in certain of our fixed maturity securities in a timely manner and adversely impact the price we receive for such securities, which may negatively impact our cash flows. Furthermore, if we experience defaults on securities held in the investment portfolios of our insurance subsidiaries, this will negatively impact statutory capital, which could reduce our insurance subsidiaries' capacity to pay dividends to our holding companies. A reduction in dividends to our holding companies could force us to seek external financing to avoid impairing our ability to pay dividends to our

stockholders or meet our debt and other payment obligations. As requirements of Dodd-Frank continue to take effect in 2015 and in subsequent years, to the extent that we enter into derivatives that are subject to centralized exchanges and cleared through a regulated clearinghouse, we may be subject to stricter collateral requirements which could have an adverse effect on our overall liquidity.

Our policy benefits are primarily in the form of claim payments, and we have minimal exposure to the policy withdrawal risk associated with deposit products such as individual life policies or annuities. A decrease in demand for our insurance products or an increase in the incidence of new claims or the duration of existing claims could negatively impact our cash flows from operations. However, our historical pattern of benefits paid to revenues is consistent, even during cycles of economic downturns, which serves to minimize liquidity risk.

Cash equivalents and marketable securities held at Unum Group and our intermediate holding companies are a significant source of liquidity for us and were approximately $575 million and $514 million at December 31, 2014 and 2013, respectively. The change was driven primarily by increases from dividends from subsidiaries and our debt issuance in March, less decreases resulting from debt repayments and repurchases of our common stock. The December 31, 2014 balance, of which approximately $176 million was held in certain of our foreign subsidiaries in the U.K., was comprised primarily of commercial paper, fixed maturity securities with a current average maturity of 1.8 years, and various money-market funds. No significant restrictions exist on our ability to use or access these funds. We currently have no intent, nor do we foresee a need, to repatriate funds from our foreign subsidiaries in the U.K. We believe we hold domestic resources sufficient to fund our liquidity requirements for the next 12 months. If we repatriate additional funds from our subsidiaries in the U.K., the amounts repatriated would be subject to repatriation tax effects which generally equal the difference in the U.S. tax rate and the U.K. tax rate.

As part of our capital deployment strategy, we have in recent years repurchased shares of Unum Group's common stock, as authorized by our board of directors. Our current share repurchase program was approved by our board of directors in December 2013 and authorizes the repurchase of up to $750 million of common stock through June 2015, with the pace of repurchase activity to depend upon various factors such as the level of available cash, alternative uses for cash, and our stock price. The dollar value of shares remaining under the current repurchase program was approximately $430 million at December 31, 2014. During 2014, we repurchased 8.7 million shares at a cost of approximately $301 million.

Cash Available from Subsidiaries

Unum Group and certain of its intermediate holding company subsidiaries depend on payments from subsidiaries to pay dividends to stockholders, to pay debt obligations, and/or to pay expenses. These payments by our insurance and non-insurance subsidiaries may take the form of dividends, operating and investment management fees, and/or interest payments on loans from the parent to a subsidiary.

Restrictions under applicable state insurance laws limit the amount of dividends that can be paid to a parent company from its insurance subsidiaries in any 12-month period without prior approval by regulatory authorities. For life insurance companies domiciled in the U.S., that limitation generally equals, depending on the state of domicile, either ten percent of an insurer's statutory surplus with respect to policyholders as of the preceding year end or the statutory net gain from operations, excluding realized investment gains and losses, of the preceding year. The payment of dividends to a parent company from a life insurance subsidiary is generally further limited to the amount of unassigned funds.

Certain of our domestic insurance subsidiaries cede blocks of business to Northwind Reinsurance Company (Northwind Re), Tailwind Reinsurance Company (Tailwind Re), and Fairwind Insurance Company (Fairwind), all of which are affiliated captive reinsurance subsidiaries domiciled in the United States with Unum Group as the ultimate parent. The ability of Northwind Re, Tailwind Re, and Fairwind to pay dividends to their respective parent companies will depend on their satisfaction of applicable regulatory requirements and on the performance of the business reinsured by Northwind Re, Tailwind Re, and Fairwind.

The ability of Unum Group and certain of its intermediate holding company subsidiaries to continue to receive dividends from their insurance subsidiaries also depends on additional factors such as RBC ratios and capital adequacy and/or solvency requirements, funding growth objectives at an affiliate level, and maintaining appropriate capital adequacy ratios to support desired ratings. Unum Group's RBC ratio for its traditional U.S. insurance subsidiaries, calculated on a weighted average basis using the NAIC Company Action Level formula, was in excess of 400 percent at December 31, 2014, and generally consistent with the prior year. The capital adequacy and/or individual RBC ratios for each of our U.S. insurance subsidiaries, including our captive reinsurers, is above the range that would require state regulatory action.

Unum Group and/or certain of its intermediate holding company subsidiaries may also receive dividends from our U.K. subsidiaries, the payment of which may be subject to applicable insurance company regulations and capital guidance in the U.K. Our European holding company and its subsidiaries, including Unum Limited, will be impacted by new capital requirements and risk management standards under Solvency II, which is expected to be adopted January 1, 2016. Solvency II proposals, which are expected to be finalized during the first quarter of 2015, contain amended requirements on capital adequacy and risk management for insurers. The impact of Solvency II on our U.K. subsidiaries cannot be fully determined at this time, but the

adoption of Solvency II will likely result in an increase in supervisory and disclosure requirements and could also result in increased capital requirements.

The payment of dividends to the parent company from our subsidiaries also requires the approval of the individual subsidiary's board of directors.

The amount available during 2014 for the payment of ordinary dividends from Unum Group's traditional U.S. insurance subsidiaries, which excludes our captive reinsurers, was $591.0 million, of which $564.0 million was declared and paid. The amount available during 2014 from Unum Limited was £187.8 million, of which £60.0 million was declared and paid to one of our U.K. holding companies. During 2014, Tailwind Re and Northwind Re paid dividends of $12.8 million and $41.3 million to Tailwind Holdings and Northwind Holdings, respectively. Fairwind paid no dividends during 2014.

During 2015, we intend to maintain a level of capital in our U.S. and U.K. insurance subsidiaries above the applicable capital adequacy requirements and minimum solvency margins. Although we may not utilize the entire amount of available dividends, based on applicable restrictions under current law, approximately $605 million is available, without prior approval by regulatory authorities, during 2015 for the payment of dividends from our traditional U.S. insurance subsidiaries, which excludes our captive reinsurers. Approximately £167 million is available for the payment of dividends from Unum Limited during 2015, subject to regulatory approval.

Insurance regulatory restrictions do not limit the amount of dividends available for distribution from non-insurance subsidiaries except where the non-insurance subsidiaries are held directly or indirectly by an insurance subsidiary and only indirectly by Unum Group.

Funding for Employee Benefit Plans

We made contributions of approximately $65.1 million and £3.1 million to our U.S. and U.K. defined contribution plans, respectively, in 2014. We expect to make contributions of approximately $68.9 million and £4.6 million during 2015. We contribute to our U.K. defined benefit pension plan sufficient to meet the minimum funding requirement under U.K. legislation and accordingly made required contributions of £1.4 million to our U.K. defined benefit pension plan during 2014. We do not expect to make contributions in 2015 to our U.K. defined benefit pension plan. We made no contributions to our U.S. qualified defined benefit pension plan during 2014, nor do we expect to make any contributions during 2015. We have met all minimum pension funding requirements set forth by the Employee Retirement Income Security Act. We have estimated our future funding requirements under the Pension Protection Act of 2006 and under applicable U.K. law, and do not believe that any future funding requirements will cause a material adverse effect on our liquidity. See Note 9 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of our employee benefit plans.

Debt

There are no significant financial covenants associated with any of our outstanding debt obligations. We continually monitor our compliance with our debt covenants and remain in compliance. We have not observed any current trends that would cause a breach of any debt covenants.

Purchases and Retirement of Debt

In 2014, we purchased and retired $145.0 million principal of our outstanding 6.85% notes, including a make-whole amount of $13.2 million, for a total cost of $158.2 million.

In 2013, we purchased and retired the outstanding principal of $62.5 million on the floating rate, senior secured non-recourse notes issued by Tailwind Holdings, resulting in a before-tax gain of $4.0 million. During 2012, Tailwind Holdings made principal payments of $10.0 million.

Northwind Holdings made principal payments on its floating rate, senior secured notes of $41.6 million in 2014 and $60.0 million in both 2013 and 2012.

Issuance of Debt

In 2014, we issued $350.0 million of unsecured 10-year senior notes in a public offering. These notes, due 2024, bear interest at a fixed rate of 4.00% and are payable semi-annually. The notes are callable at or above par and rank equally in right of payment with all of our other unsecured and unsubordinated debt.

In 2012, we issued $250.0 million of unsecured senior notes in a public offering. These notes, due 2042, bear interest at a fixed rate of 5.75% and are payable semi-annually. The notes are callable at or above par and rank equally in right of payment with all of our other unsecured and unsubordinated debt.

Credit Facility

In 2013, we entered into a five-year, $400 million unsecured revolving credit facility. Under the terms of the agreement, we may request that the credit facility be increased up to $600 million. Borrowings under the credit facility are for general corporate uses and are subject to financial covenants, negative covenants, and events of default that are customary. The credit facility provides for borrowing at an interest rate based either on the prime rate or LIBOR. In addition, the credit facility provides for the issuance of letters of credit subject to certain terms and limitations. At December 31, 2014, letters of credit totaling $2.1 million had been issued from the credit facility, but there was no borrowed amount outstanding. Our credit facility's financial covenants contain provisions regarding our leverage and net worth. We do not anticipate any violation of these covenants. However, if economic conditions worsen and we incur unexpected losses, we could violate certain of the financial covenants imposed by the credit facility and lose access to available funds or lines of credit through the facility. While maintenance of the unsecured, revolving credit facility provides a valuable source of contingent liquidity, we believe operating cash flows are sufficient to support our short-term liquidity needs.

Shelf Registration

We filed a shelf registration with the Securities and Exchange Commission in 2014 to issue various types of securities, including common stock, preferred stock, debt securities, depository shares, stock purchase contracts, units and warrants, or preferred securities of wholly-owned finance trusts. The shelf registration enables us to raise funds from the offering of any securities covered by the shelf registration as well as any combination thereof, subject to market conditions and our capital needs.

See Note 8 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for additional information on our debt.

Commitments

The following table summarizes contractual obligations and our reinsurance recoverable by period as of December 31, 2014:

(in millions of dollars)

	Total	In 1 Year or Less	After 1 Year up to 3 Years	After 3 Years up to 5 Years	After 5 Years
Payments Due					
Short-term Debt	$161.0	$161.0	$—	$—	$—
Long-term Debt	4,321.8	136.1	597.9	412.8	3,175.0
Policyholder Liabilities	43,358.3	4,685.3	6,864.5	5,394.8	26,413.7
Pension and OPEB	725.7	19.5	38.2	37.3	630.7
Miscellaneous Liabilities	687.8	613.6	18.0	11.8	44.4
Operating Leases	227.1	40.2	75.6	35.7	75.6
Purchase Obligations	256.7	254.6	2.1	—	—
Total	$49,738.4	$5,910.3	$7,596.3	$5,892.4	$30,339.4
Receipts Due					
Reinsurance Recoverable	$7,704.9	$348.9	$605.5	$615.3	$6,135.2

Short-term and long-term debt includes contractual principal and interest payments and therefore exceeds the amount shown in the consolidated balance sheets.

Policyholder liability maturities and the related reinsurance recoverable represent the projected payout of the current in-force policyholder liabilities and the expected cash inflows from reinsurers for liabilities ceded and therefore incorporate uncertainties as to the timing and amount of claim payments. We utilize extensive liability modeling to project future cash flows from the in-force business. The primary assumptions used to project future cash flows are claim incidence rates for mortality and morbidity, claim resolution rates, persistency rates, and interest rates. These cash flows are discounted to determine the current value of the projected claim payments. The timing and amount of payments on policyholder liabilities may vary significantly from the projections above.

Pensions and OPEB commitments represent the expected benefit payments related to our U.S. non-qualified defined benefit pension and other postretirement benefit plans as it is our policy to pay those benefits, as incurred, from our general assets. Our funding policy for our U.S. qualified defined benefit and our U.K. defined benefit pension plans is to make only contributions necessary to meet minimum funding requirements under U.S. and U.K. legislation. We do not currently expect to make any contributions to either of these plans and therefore have not included amounts in the preceding chart. However, to the extent contributions are required, we will make the necessary contributions to these plans.

Miscellaneous liabilities include commissions due and accrued, deferred compensation liabilities, state premium taxes payable, amounts due to reinsurance companies, obligations to return unrestricted cash collateral to our securities lending and derivatives counterparties, legally binding commitments to fund investments, and various other liabilities that represent contractual obligations. Obligations where the timing of the payment is uncertain are included in the one year or less category.

See "Critical Accounting Estimates" contained in this Item 7 and Notes 3, 4, 6, 8, 9, and 14 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for additional information on our various commitments and obligations.

Off-Balance Sheet Arrangements

Operating leases include noncancelable obligations on certain office space, equipment, and software. Purchase obligations include non-binding commitments of $238.4 million to fund certain of our investments. These are included in the preceding table based on the expiration date of the commitments. The funds are due upon satisfaction of contractual notice from appropriate external parties and may or may not be funded. Also included are obligations with outside parties for computer data processing services, software maintenance agreements, and consulting services. The aggregate obligation remaining under these agreements was $16.8 million at December 31, 2014.

As part of our regular investing strategy, we receive collateral from unaffiliated third parties through transactions which include both securities lending and also short-term agreements to purchase securities with the agreement to resell them at a later specified date. For both types of transactions, we require that a minimum of 102 percent of the fair value of the securities loaned or securities purchased under repurchase agreements be maintained as collateral. Generally, cash is received as collateral under these agreements. In the event that securities are received as collateral, we are not permitted to sell or re-post them. We also post our fixed maturity securities as collateral to unaffiliated third parties through transactions including both securities lending and also short-term agreements to sell securities with the agreement to repurchase them at a later specified date. See "Transfers of Financial Assets" as follows for further discussion.

To help limit the credit exposure of derivatives, we enter into master netting agreements with our counterparties whereby contracts in a gain position can be offset against contracts in a loss position. We also typically enter into bilateral, cross-collateralization agreements with our counterparties to help limit the credit exposure of the derivatives. These agreements require the counterparty in a loss position to submit acceptable collateral with the other counterparty in the event the net loss position meets or exceeds an agreed upon amount. Our current credit exposure on derivatives, which is limited to the value of those contracts in a net gain position, including accrued interest receivable less collateral held, was $13.6 million at December 31, 2014. We held cash collateral from our counterparties of $15.4 million at December 31, 2014 and had posted fixed maturity securities with a carrying value of $67.0 million as collateral to our counterparties.

See Notes 3, 4, and 14 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for additional information.

Transfers of Financial Assets

Our investment policy permits us to lend fixed maturity securities to unaffiliated financial institutions in short-term securities lending agreements, which increase our investment income with minimal risk. We account for all of our securities lending agreements and repurchase agreements as secured borrowings. We had $58.4 million of securities lending agreements outstanding which were collateralized by cash at December 31, 2014 and were reported as other liabilities in our consolidated balance sheets. The cash received as collateral was reinvested in short-term investments. The average balance during the year ended December 31, 2014 was $65.5 million, and the maximum amount outstanding at any month end was $94.0 million. In addition, at December 31, 2014, we had $128.5 million of off-balance sheet securities lending agreements which were collateralized by securities that we were neither permitted to sell nor control. The average balance of these off-balance sheet transactions during the year ended December 31, 2014 was $116.5 million, and the maximum amount outstanding at any month end was $153.6 million.

We had no repurchase agreements outstanding at December 31, 2014. The average balance during the year ended December 31, 2014 was $1.6 million, and the maximum amount outstanding at any month end was $12.8 million. Our use of repurchase agreements and securities lending agreements can fluctuate during any given period and will depend on our liquidity position, the availability of long-term investments that meet our purchasing criteria, and our general business needs.

During 2014, we were approved for membership of the Federal Home Loan Bank System (FHLB). As a member, we obtain access to low-cost funding and also receive dividends based on our stock ownership. Membership requires that we purchase a minimum amount of FHLB common stock based on a percentage of our total assets. Additional common stock purchases are required based upon the amount of funds borrowed from the FHLB. We will be required to post mortgage-related assets, U.S. Treasury securities, or other acceptable forms of collateral for any borrowings we make from the FHLB. As of December 31, 2014 we had not funded any FHLB common stock purchases or obtained any advances from the FHLB. Our initial common stock membership purchase will be funded in the first quarter of 2015.

See Note 3 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for additional information.

Consolidated Cash Flows
(in millions of dollars)

	Year Ended December 31		
	2014	2013	2012
Net Cash Provided by Operating Activities	$1,223.6	$1,031.5	$1,379.6
Net Cash Used by Investing Activities	(886.6)	(419.2)	(969.9)
Net Cash Used by Financing Activities	(328.6)	(595.5)	(449.0)
Net Increase (Decrease) in Cash and Bank Deposits	$8.4	$16.8	$(39.3)

Operating Cash Flows
Operating cash flows are primarily attributable to the receipt of premium and investment income, offset by payments of claims, commissions, expenses, and income taxes. Premium income growth is dependent not only on new sales, but on policy renewals and growth of existing business, renewal price increases, and persistency. Investment income growth is dependent on the growth in the underlying assets supporting our insurance reserves and capital and on the earned yield. The level of commissions and operating expenses is attributable to the level of sales and the first year acquisition expenses associated with new business as well as the maintenance of existing business. The level of paid claims is affected partially by the growth and aging of the block of business and also by the general economy, as previously discussed in the operating results by segment.

The variance in the change in insurance reserves and liabilities to reconcile net income to net cash provided by operating activities as reported in our consolidated statements of cash flows for 2014 compared to the prior two years was due primarily to the 2014 reserve increase for our long-term care line of business.

Investing Cash Flows

Investing cash inflows consist primarily of the proceeds from the sales and maturities of investments. Investing cash outflows consist primarily of payments for purchases of investments. Our investment strategy is to match the cash flows and durations of our assets with the cash flows and durations of our liabilities to meet the funding requirements of our business. When market opportunities arise we may sell selected securities and reinvest the proceeds to improve the yield and credit quality of our portfolio, as was the case during 2013 when we sold lower yielding fixed maturity securities to take advantage of the higher interest rate environment by reinvesting the proceeds into higher yielding mortgage-backed and corporate securities with a higher credit quality. We may at times also sell selected securities and reinvest the proceeds to improve the duration matching of our assets and liabilities and/or re-balance our portfolio. As a result, sales before maturity may vary from period to period. The sale and purchase of short-term investments is influenced by our securities lending program and by the amount of cash which is at times held in short-term investments to facilitate the availability of cash to fund the purchase of appropriate long-term investments and/or to fund our capital deployment program.

See Notes 3 and 4 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further information.

Financing Cash Flows

Financing cash flows consist primarily of borrowings and repayments of debt, issuance or repurchase of common stock, and dividends paid to stockholders.

During 2014, we retired $145.0 million principal of our outstanding 6.85% notes, including a make-whole amount of $13.2 million, for a total cash outflow of $158.2 million. During 2014, 2013, and 2012 we made principal payments of $41.6 million, $60.0 million, and $60.0 million, respectively, on our senior secured non-recourse notes issued by

Northwind Holdings. During 2013, we purchased and retired the outstanding principal of $62.5 million on our floating rate, senior secured non-recourse notes issued by Tailwind Holdings for $56.2 million. During 2012, we made principal payments of $10.0 million on the Tailwind Holdings notes.

During 2014, we issued $350.0 million of 4.00% unsecured 10-year senior notes in a public offering and received proceeds of $347.2 million, excluding the associated debt issuance costs and discounts. During 2012, we issued $250.0 million of 5.75% senior notes and received proceeds of $246.4 million, excluding the associated debt issuance costs and discounts.

Cash used to repurchase shares of Unum Group's common stock during 2014, 2013, and 2012 was $306.0 million, $317.2 million, and $496.7 million, respectively. During 2014, 2013, and 2012 we paid dividends of $159.4 million, $146.5 million, and $133.8 million, respectively, to holders of Unum Group's common stock.

See "Debt" contained in this Item 7, and Notes 8 and 10 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further information.

Ratings

AM Best, Fitch, Moody's, and S&P are among the third parties that assign issuer credit ratings to Unum Group and financial strength ratings to our insurance subsidiaries. We compete based in part on the financial strength ratings provided by rating agencies. A downgrade of our financial strength ratings can be expected to adversely affect us and could potentially, among other things, adversely affect our relationships with distributors of our products and services and retention of our sales force, negatively impact persistency and new sales, particularly large case group sales and individual sales, and generally adversely affect our ability to compete. A downgrade in the issuer credit rating assigned to Unum Group can be expected to adversely affect our cost of capital or our ability to raise additional capital.

The table below reflects the outlook as well as the issuer credit ratings for Unum Group and the financial strength ratings for each of our traditional insurance subsidiaries as of the date of this filing.

	AM Best	Fitch	Moody's	S&P
Outlook	Stable	Stable	Stable	Stable
Issuer Credit Ratings	bbb	BBB	Baa2	BBB
Financial Strength Ratings				
Provident Life and Accident	A	A	A2	A
Provident Life and Casualty	A	A	NR	NR
Unum Life of America	A	A	A2	A
First Unum Life	A	A	A2	A
Colonial Life & Accident	A	A	A2	A
Paul Revere Life	A	A	A2	A
Paul Revere Variable	B++	A	A2	NR
Unum Limited	NR	NR	NR	A-

NR = not rated

We maintain an ongoing dialogue with the four rating agencies that evaluate us in order to inform them of progress we are making regarding our strategic objectives and financial plans as well as other pertinent issues. A significant component of our communications involves our annual review meeting with each of the four agencies. We hold other meetings throughout the year regarding our business, including, but not limited to, quarterly updates.

On December 16, 2014, Fitch affirmed its A rating of our domestic insurance subsidiaries and affirmed the BBB issuer credit rating for Unum Group following our 2015 Outlook Meeting held that day during which we discussed our expected long-term care reserve charge. On December 19, 2014, AM Best also affirmed its A rating of our primary domestic insurance subsidiaries and affirmed the senior debt rating of Unum Group at bbb. There have been no changes in any of the rating agencies' outlook statements or ratings during 2014 or 2015 prior to the date of this filing.

85

Agency ratings are not directed toward the holders of our securities and are not recommendations to buy, sell, or hold our securities. Each rating is subject to revision or withdrawal at any time by the assigning rating organization, and each rating should be regarded as an independent assessment, not conditional on any other rating. Given the dynamic nature of the ratings process, changes by these or other rating agencies may or may not occur in the near-term. Based on our ongoing dialogue with the rating agencies concerning our insurance risk profile, our financial flexibility, our operating performance, and the quality of our investment portfolio, we do not expect any negative actions from any of the four rating agencies related to either Unum Group's current issuer credit ratings or the financial strength ratings of our insurance subsidiaries. However, in the event that we are unable to meet the rating agency specific guideline values to maintain our current ratings, including but not limited to maintenance of our capital management metrics at the threshold values stated and maintenance of our financial flexibility and operational consistency, we could be placed on a negative credit watch, with a potential for a downgrade to both our issuer credit ratings and our financial strength ratings.

See "Ratings" contained herein in Item 1 and "Risk Factors" contained herein in Item 1A for further discussion.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are subject to various market risk exposures, including interest rate risk and foreign exchange rate risk. The following discussion regarding our risk management activities includes forward-looking statements that involve risk and uncertainties. Estimates of future performance and economic conditions are reflected assuming certain changes in market rates and prices were to occur (sensitivity analysis). Caution should be used in evaluating our overall market risk from the information presented below, as actual results may differ. See "Risk Factors" contained herein in Item 1A, "Investments" contained herein in Item 7, and Notes 2, 3, and 4 of the "Notes to Consolidated Financial Statements" contained herein in Item 8 for further discussion of the qualitative aspects of market risk, including derivative financial instrument activity.

Interest Rate Risk

Our exposure to interest rate changes results from our holdings of financial instruments such as fixed rate investments, derivatives, and interest-sensitive liabilities. Fixed rate investments include fixed maturity securities, mortgage loans, policy loans, and short-term investments. Fixed maturity securities include U.S. and foreign government bonds, securities issued by government agencies, public utility bonds, corporate bonds, mortgage-backed securities, and redeemable preferred stock, all of which are subject to risk resulting from interest rate fluctuations. Certain of our financial instruments, fixed maturity securities and derivatives, are carried at fair value in our consolidated balance sheets. The fair value of these financial instruments may be adversely affected by changes in interest rates. A rise in interest rates may decrease the net unrealized gain related to these financial instruments, but may improve our ability to earn higher rates of return on new purchases of fixed maturity securities. Conversely, a decline in interest rates may increase the net unrealized gain, but new securities may be purchased at lower rates of return. Although changes in fair value of fixed maturity securities and derivatives due to changes in interest rates may impact amounts reported in our consolidated balance sheets, these changes will not cause an economic gain or loss unless we sell investments, terminate derivative positions, determine that an investment is other than temporarily impaired, or determine that a derivative instrument is no longer an effective hedge.

Other fixed rate investments, such as mortgage loans and policy loans, are carried at amortized cost and unpaid balances, respectively, rather than fair value in our consolidated balance sheets. These investments may have fair values substantially higher or lower than the carrying values reflected in our balance sheets. A change in interest rates could impact our financial position if we sold our mortgage loan investments at times of low market value. A change in interest rates would not impact our financial position at repayment of policy loans, as ultimately the cash surrender values or death benefits would be reduced for the carrying value of any outstanding policy loans. Carrying amounts for short-term investments approximate fair value, and we believe we have minimal interest rate risk exposure from these investments.

We believe that the risk of being forced to liquidate investments or terminate derivative positions is minimal, primarily due to the level of capital at our insurance subsidiaries, the level of cash and marketable securities at our holding companies, and our investment strategy which we believe provides for adequate cash flows to meet the funding requirements of our business. We may in certain circumstances, however, need to sell investments due to changes in regulatory or capital requirements, changes in tax laws, rating agency decisions, and/or unexpected changes in liquidity needs.

Although our policy benefits are primarily in the form of claim payments and we therefore have minimal exposure to the policy withdrawal risk associated with deposit products such as individual life policies or annuities, the fair values of liabilities under all insurance contracts are taken into consideration in our overall management of interest rate risk, which minimizes exposure to changing interest rates through the matching of investment cash flows with amounts due under insurance contracts. Changes in interest rates and individuals' behavior affect the amount and timing of asset

and liability cash flows. We actively manage our asset and liability cash flow match and our asset and liability duration match to limit interest rate risk. Due to the long duration of our long-term care product, the timing and/or amount of our investment cash flows may not match those of our maturing liabilities. We model and test asset and liability portfolios to improve interest rate risk management and net yields. Testing the asset and liability portfolios under various interest rate and economic scenarios enables us to choose what we believe to be the most appropriate investment strategy, as well as to limit the risk of disadvantageous outcomes. We use this analysis in determining hedging strategies and utilizing derivative financial instruments. We use current and forward interest rate swaps, options on forward interest rate swaps, and forward treasury locks to hedge interest rate risks and to match asset durations and cash flows with corresponding liabilities.

Debt is not carried at fair value in our consolidated balance sheets. If we modify or replace existing debt instruments at current market rates, we may incur a gain or loss on the transaction. We believe our debt-related risk to changes in interest rates is relatively minimal. In the near term, we expect that our need for external financing is small, but changes in our business could increase our need.

We measure our financial instruments' market risk related to changes in interest rates using a sensitivity analysis. This analysis estimates potential changes in fair values as of December 31, 2014 and 2013 based on a hypothetical immediate increase of 100 basis points in interest rates from year end levels. The selection of a 100 basis point immediate parallel change in interest rates should not be construed as our prediction of future market events, but only as an illustration of the potential effect of such an event.

The hypothetical potential changes in fair value of our financial instruments at December 31, 2014 and 2013 are shown as follows:

(in millions of dollars)	December 31, 2014			
	Notional Amount of Derivatives	Fair Value	Hypothetical FV + 100 BP	Change in FV
Assets				
Fixed Maturity Securities (1)		$45,064.9	$41,394.8	$(3,670.1)
Mortgage Loans		2,024.2	1,931.3	(92.9)
Policy Loans, Net of Reinsurance Ceded		339.2	313.2	(26.0)
Liabilities				
Unrealized Adjustment to Reserves, Net of Reinsurance Ceded and Deferred Acquisition Costs (2)		$(5,836.1)	$(3,071.9)	$2,764.2
Short-term Debt		(158.9)	(157.8)	1.1
Long-term Debt		(2,912.6)	(2,745.6)	167.0
Derivatives (1)				
Swaps	$1,687.4	$(64.9)	$(86.8)	$(21.9)
Embedded Derivative in Modified Coinsurance Arrangement		(49.9)	(55.6)	(5.7)

(in millions of dollars)	December 31, 2013			
	Notional Amount of Derivatives	Fair Value	Hypothetical FV + 100 BP	Change in FV
Assets				
Fixed Maturity Securities (1)		$42,344.4	$39,009.2	$(3,335.2)
Mortgage Loans		1,980.2	1,889.9	(90.3)
Policy Loans, Net of Reinsurance Ceded		295.9	278.0	(17.9)
Liabilities				
Unrealized Adjustment to Reserves, Net of Reinsurance Ceded and Deferred Acquisition Costs (2)		$(3,886.3)	$(1,568.7)	$2,317.6
Long-term Debt		(2,824.4)	(2,660.5)	163.9
Derivatives (1)				
Swaps	$1,477.4	$(124.8)	$(139.7)	$(14.9)
Embedded Derivative in Modified Coinsurance Arrangement		(53.2)	(62.1)	(8.9)

(1) These financial instruments are carried at fair value in our consolidated balance sheets. Changes in fair value resulting from changes in interest rates may affect the fair value at which the item is reported in our consolidated balance sheets. The corresponding offsetting change is reported in other comprehensive income or loss, net of deferred taxes, except for changes in the fair value of derivatives accounted for as fair value hedges or derivatives not designated as hedging instruments, the offset of which is reported as a component of net realized investment gain or

loss.

(2) The adjustment to reserves and deferred acquisition costs for unrealized investment gains and losses reflects the adjustments to policyholder liabilities and deferred acquisition costs that would be necessary if the unrealized investment gains and losses related to the fixed maturity securities and derivatives had been realized. Changes in this adjustment are also reported as a component of other comprehensive income or loss, net of deferred taxes.

The effect of a change in interest rates on asset prices was determined using a duration implied methodology for corporate bonds and government and government agency securities whereby the duration of each security was used to estimate the change in price for the security assuming an increase of 100 basis points in interest rates. The effect of a change in interest rates on the mortgage-backed securities was estimated using a mortgage analytic system which takes into account the impact of changing prepayment speeds resulting from a 100 basis point increase in interest rates on the change in price of the mortgage-backed securities. These hypothetical prices were compared to the actual prices for the period to compute the overall change in market value. The changes in the fair values shown in the chart above for all other items were determined using discounted cash flow analyses. Because we actively manage our investments and liabilities, actual changes could be less than those estimated above.

Sustained periods of low interest rates may result in lower than expected profitability. Assuming interest rates and credit spreads remained constant throughout 2015 at the January 2015 market levels, our net investment income would decrease by approximately $1 million in 2015 and $7 million in 2016 relative to our current expectations. This interest rate scenario does not give consideration to the effect of other factors which could impact these results, such as changes in the bond market and changes in hedging strategies and positions, nor does it consider the potential change to our discount rate reserve assumptions and any mitigating factors such as pricing adjustments. In addition, a continued low or declining interest rate environment may also result in an increase in the net periodic benefit costs for our pension plans, but we do not believe it would materially affect net income in 2015 or 2016.

Foreign Currency Risk

The functional currency of our U.K. operations is the British pound sterling. We are exposed to foreign currency risk arising from fluctuations in the British pound sterling to U.S. dollar exchange rates primarily as they relate to the translation of the financial results of our U.K. operations. Fluctuations in the pound to dollar exchange rate have an effect on our reported financial results. We do not hedge against the possible impact of this risk. Because we do not actually convert pounds into dollars except for a limited number of transactions, we view foreign currency translation as a financial reporting issue and not a reflection of operations or profitability in our U.K. operations.

Assuming the pound to dollar exchange rate decreased 10 percent from the December 31, 2014 and 2013 levels, stockholders' equity as reported in U.S. dollars would have been lower by approximately $100 million at each of those year end periods. Assuming the pound to dollar average exchange rate decreased 10 percent from the actual average exchange rates for 2014 and 2013, before-tax operating income, as reported in U.S. dollars, would have decreased approximately $15 million in each of those two years.

Dividends paid by Unum Limited are generally held at our U.K. finance subsidiary or our U.K. holding company. If these funds are repatriated to our U.S. holding company, we would at that time be subject to foreign currency risk as the value of the dividend, when converted into U.S. dollars, would be dependent upon the foreign exchange rate at the time of conversion.

We are also exposed to foreign currency risk related to certain foreign investment securities denominated in local currencies and U.S. dollar-denominated debt issued by one of our U.K. subsidiaries. We use current and forward currency swaps to hedge or minimize the foreign exchange risk associated with these instruments.

See "Risk Factors" contained herein in Item 1A and "Consolidated Operating Results" and "Unum UK Segment" contained herein in Item 7 for further information concerning foreign currency translation.

Risk Management

Effectively taking and managing risks is essential to the success of our Company. To facilitate this effort, we have a formal Enterprise Risk Management (ERM) program, with a framework comprising the following key components:

- Risk culture and governance
- Risk appetite policy
- Risk identification and prioritization
- Risk and capital modeling
- Risk management activities
- Risk reporting

Our ERM framework is the ongoing system of people, processes, and tools across our Company under which we intend to function consistently and collectively to identify and assess risks and opportunities, to manage all material risks within our risk appetite, and to contribute to strategic decision making. With the goal of maximizing shareholder value, the primary objectives of our ERM framework are to support Unum Group in meeting its operational and financial objectives, maintaining liquidity, optimizing capital, and protecting franchise value.

Risk Culture and Governance

We employ a decentralized risk management model under which risk-based decisions are made daily on a local level. To achieve long-term success, we believe risk management must be the responsibility of all employees. The individual and collective decisions of our employees play a key role in successfully managing our overall risk profile. We strive for a culture of accountability, risk management, and strict compliance, and we believe these values allow our employees to feel comfortable identifying issues as well as taking ownership for addressing potential problems.

Our risk culture is reinforced by our system of risk governance. We employ a multi-layered risk control system. Our three lines of defense model is depicted below.

1st Line: Own and Manage	2nd Line: Oversee	3rd Line: Independent Assurance
Business processes and procedures employed throughout the Company through which management assumes and monitors significant risks	Management committees chartered with oversight of activities within the 1st and 2nd lines of defense, mitigation of substantial exposures, and management of emerging risks	Independent review of ERM framework and risk mitigation

Business units are primarily responsible for managing their principal risks. Our risk committees and other management committees serve risk and control functions responsible for providing risk oversight, or the second line of risk control. The internal audit team provides a second level of independent review, or our third line of risk control. The risk and finance committee of Unum Group's board of directors (the board) oversees the entire ERM governance process, effectively providing independent review for our third line of risk control.

The board has an active role, as a whole and through its committees, in overseeing management of our risks. The board is responsible for managing strategic risk and regularly reviews information regarding our capital, liquidity, and operations, as well as the risks associated with each. The risk and finance committee of the board is responsible for oversight of our risk management process, including financial risk, operational risk, and any other risk not specifically assigned to another board committee. It also is responsible for oversight of risks associated with investments, capital and financing plans and activities, and related financial matters, including matters pertaining to our Closed Block segment. The audit committee of the board is responsible for oversight of risks relating to financial reporting risk and certain operational risks. The human capital committee of the board is responsible for oversight of risks relating to our compensation plans and programs. The regulatory compliance committee of the board is responsible for oversight of risks related to regulatory, compliance, policy, and legal matters, both current and emerging, and whether of a local, state, federal, or international nature. While each committee is responsible for evaluating certain risks and overseeing the management of such risks, the entire board is regularly informed through committee reports about such risks in addition to the risk information it receives directly.

The executive risk management committee is responsible for overseeing our enterprise-wide risk management program. The chief risk officer, who is a member of the executive risk management committee, has primary responsibility for our ERM program and is supported by corporate risk committees and by the risk committees of our primary operating segments.

Operating segment risk committees for Unum US, Unum UK, Colonial Life, and Closed Block are responsible for oversight of risks specific to their businesses. These committees are responsible for identifying, measuring, reporting, and managing insurance and operational risks within their respective areas, consistent with enterprise risk management guidance. Corporate risk committees and other management committees oversee the operational, global technology services, investment, and capital management risks on a corporate level.

Risk Appetite Policy

Our risk appetite policy describes the types of risks we are willing to take, as well as the amount of enterprise risk exposure we deem acceptable in pursuit of our goals, with an objective of clearly defining boundaries for our risk-taking activities.

The starting point of our philosophy and approach to our ERM strategy is our corporate strategy. In contrast to many multi-line peer companies, we do not offer retirement savings, traditional medical benefits, or property and casualty insurance. Our corporate strategy is focused on providing group, individual, and voluntary benefits, either as stand-alone products or combined with other coverages, that create comprehensive benefits solutions for employers. We have market leadership positions in the product lines we offer and believe this combination of focused expertise and experience is a competitive advantage and forms the foundation of our approach to risk management.

We believe our sound and consistent business practices, strong internal compliance program, and comprehensive risk management strategy enable us to operate efficiently and to identify and address potential areas of risk in our business. We take and manage risks to achieve our business and strategic objectives, and our risk appetite statement sets boundaries for risk-taking activities that link earnings, capital, and operational processes, as well as summarizes our most material risk limits and controls. We monitor our risk profile against our established risk tolerance and limits. Risks falling outside our risk tolerance and limits are reported to the applicable governance group, where decisions are made pertaining to acceptance of the risk or implementation of remediation plans or corrective actions as deemed appropriate by that governance group.

Risk Identification and Prioritization

Risk identification and prioritization is an ongoing process, whereby we identify and assess our risk positions and exposures, including notable risk events. Additionally, we identify emerging risks and analyze how material future risks might affect us. Knowing the potential risks we face allows us to monitor and manage their potential effects including adjusting our strategies as appropriate and holding capital levels which provide financial flexibility. Risk and other management committees have primary responsibility for identifying and prioritizing risks within their respective areas.

We face a wide range of risks, and our continued success depends on our ability to identify and appropriately manage our risk exposures. For additional information on certain risks that may adversely affect our business, operating results, or financial condition see "Cautionary Statement Regarding Forward-Looking Statements" contained herein on page 1 and "Risk Factors" contained herein in Item 1A.

Risk and Capital Modeling

We assess material risks, including how they affect us and how individual risks interrelate, to provide valuable information to management in order that they may effectively manage our risks. We use qualitative and quantitative approaches to assess existing and emerging risks and to develop mitigating strategies to limit our exposure to both.

We utilize stress testing and scenario analysis for risk management and to shape our business, financial, and strategic planning activities. Both are key components of our risk appetite policy and play an important role in monitoring, assessing, managing, and mitigating our primary risk exposures.
In particular, stress testing of our capital and liquidity management strategies enables us to identify areas of high exposure, assess mitigating actions, develop contingency plans, and guide decisions around our target capital and liquidity levels. For example, we periodically perform stress tests on certain categories of assets or liabilities to support development of capital and liquidity risk contingency plans. These tests help ensure that we have a buffer to

support our operations in uncertain times and financial flexibility to respond to market opportunities. Stress testing is also central to reserve adequacy testing, cash flow testing, and asset and liability management.

In addition, we aim to constantly improve our capital modeling techniques and methodologies that are used to determine a level of capital that is commensurate with our risk profile and to ensure compliance with evolving regulatory and rating agency requirements. Our capital modeling reflects appropriate aggregation of risks and diversification benefits resulting from our mix of products and business units.

Our internal capital modeling and allocation aids us in making significant business decisions including strategic planning, capital management, risk limit determination, reinsurance purchases, hedging activities, asset allocation, pricing, and corporate development.

Risk Management Activities

We accept and manage strategic, credit, and insurance risks in accordance with our corporate strategy, investment policy, and annual business plans. The following fundamental principles are embedded in our risk management efforts across our Company.

- We believe in the benefits of specialization and a focused business strategy. We seek profitable risk-taking in areas where we have established risk management skills and capabilities.
- We seek to manage our exposure to insurance risk through a combination of prudent underwriting with effective risk selection, maintaining pricing discipline, sound reserving practices, and claims operational effectiveness. Detailed underwriting guidelines and claim policies are tools used to manage our insurance risk exposure. We also monitor exposures against internally prescribed limits, and we diversify to reduce potential concentration risk and volatility.
- We maintain a detailed set of investment policies and guidelines, including fundamental credit analysis, that are used to manage our credit risk exposure and diversify our risks across asset classes and issuers.
- Finally, we foster a risk culture that embeds our corporate values and our code of conduct in our daily operations and preserves our reputation with customers and other key stakeholders. We monitor a composite set of operational risk metrics that measure operating effectiveness from the customer perspective.

Risk Reporting

Regular internal and external risk reporting is an integral part of our ERM framework. Internally, ERM reports are a standard part of our quarterly senior management and board meetings. The reports summarize our existing and emerging risk exposures, as well as report against the tolerances and limits defined by our risk appetite policy.

Externally, we are subject to a number of regulatory and rating agency risk examinations, and risk reports are often included. During 2015, we must comply with the ORSA requirements, which are intended to become a regular part of reviews of insurers' ERM programs. We believe the ORSA will provide strong evidence of the strengths of our ERM framework, measurement approaches, key assumptions utilized in assessing our risks, and prospective solvency assessments under both normal and stressed conditions. We have implemented, and will continue to implement, actions to prepare for compliance with this standard. See "Regulation" contained herein in Item 1 for additional information regarding the ORSA.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Unum Group

We have audited the accompanying consolidated balance sheets of Unum Group and subsidiaries as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2014. Our audits also included the financial statement schedules listed in the Index at Item 15(a)(2). These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Unum Group and subsidiaries at December 31, 2014 and 2013, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Unum Group and subsidiaries' internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework), and our report dated February 25, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chattanooga, Tennessee
February 25, 2015

93

CONSOLIDATED BALANCE SHEETS

Unum Group and Subsidiaries

	December 31	
	2014	2013
	(in millions of dollars)	
Assets		
Investments		
Fixed Maturity Securities - at fair value (amortized cost: $38,803.4; $38,289.6)	$45,064.9	$42,344.4
Mortgage Loans	1,856.6	1,815.1
Policy Loans	3,306.6	3,276.0
Other Long-term Investments	591.9	566.0
Short-term Investments	974.3	913.4
Total Investments	51,794.3	48,914.9
Other Assets		
Cash and Bank Deposits	102.5	94.1
Accounts and Premiums Receivable	1,634.7	1,647.8
Reinsurance Recoverable	4,906.4	4,806.5
Accrued Investment Income	696.1	700.2
Deferred Acquisition Costs	1,901.3	1,829.2
Goodwill	198.7	200.9
Property and Equipment	531.7	511.9
Income Tax Receivable	69.5	50.3
Other Assets	661.9	647.8
Total Assets	$62,497.1	$59,403.6

See notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS - Continued

Unum Group and Subsidiaries

	December 31	
	2014	2013
	(in millions of dollars)	
Liabilities and Stockholders' Equity		
Liabilities		
Policy and Contract Benefits	$1,529.3	$1,511.0
Reserves for Future Policy and Contract Benefits	45,929.4	43,099.1
Unearned Premiums	396.6	413.8
Other Policyholders’ Funds	1,657.8	1,658.4
Deferred Income Tax	78.4	144.3
Short-term Debt	151.9	—
Long-term Debt	2,628.7	2,612.0
Other Liabilities	1,572.6	1,305.9
Total Liabilities	53,944.7	50,744.5
Commitments and Contingent Liabilities - Note 14		
Stockholders' Equity		
Common Stock, $0.10 par		
Authorized: 725,000,000 shares		
Issued: 301,834,556 and 360,802,426 shares	30.2	36.1
Additional Paid-in Capital	2,221.2	2,634.1
Accumulated Other Comprehensive Income	166.4	255.0
Retained Earnings	7,332.8	8,083.2
Treasury Stock - at cost: 49,524,849 and 100,785,012 shares	(1,198.2)	(2,349.3)
Total Stockholders' Equity	8,552.4	8,659.1
Total Liabilities and Stockholders' Equity	$62,497.1	$59,403.6

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

Unum Group and Subsidiaries

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars, except share data)		
Revenue			
Premium Income	$7,797.2	$7,624.7	$7,716.1
Net Investment Income	2,477.4	2,492.1	2,515.2
Realized Investment Gain (Loss)			
Other-Than-Temporary Impairment Loss on Fixed Maturity Securities	(13.5)	(0.8)	—
Other Net Realized Investment Gain	29.6	7.6	56.2
Net Realized Investment Gain	16.1	6.8	56.2
Other Income	219.0	230.2	227.9
Total Revenue	10,509.7	10,353.8	10,515.4
Benefits and Expenses			
Benefits and Change in Reserves for Future Benefits	7,310.8	6,595.7	6,722.2
Commissions	935.3	909.5	917.2
Interest and Debt Expense	167.5	149.4	145.4
Deferral of Acquisition Costs	(524.0)	(466.8)	(467.3)
Amortization of Deferred Acquisition Costs	440.8	418.9	378.7
Compensation Expense	820.9	790.4	786.8
Other Expenses	831.2	751.5	782.9
Total Benefits and Expenses	9,982.5	9,148.6	9,265.9
Income Before Income Tax	527.2	1,205.2	1,249.5
Income Tax			
Current	103.3	296.6	206.6
Deferred	10.5	50.5	148.5
Total Income Tax	113.8	347.1	355.1
Net Income	$413.4	$858.1	$894.4
Net Income Per Common Share			
Basic	$1.62	$3.24	$3.18
Assuming Dilution	$1.61	$3.23	$3.17

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Unum Group and Subsidiaries

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Net Income	$413.4	$858.1	$894.4
Other Comprehensive Income (Loss)			
Change in Net Unrealized Gain on Securities Before Adjustment (net of tax expense (benefit) of $725.8; $(1,102.8); $467.7)	1,439.3	(2,101.2)	918.8
Change in Adjustment to Deferred Acquisition Costs and Reserves for Future Policy and Contract Benefits, Net of Reinsurance (net of tax expense (benefit) of $(665.1); $743.3; $(325.6))	(1,284.7)	1,363.4	(660.1)
Change in Net Gain on Cash Flow Hedges (net of tax benefit of $2.0; $1.3; $4.3)	(5.3)	(5.3)	(7.1)
Change in Foreign Currency Translation Adjustment	(66.3)	25.5	45.0
Change in Unrecognized Pension and Postretirement Benefit Costs (net of tax expense (benefit) of $(92.4); $185.2; $(68.0))	(171.6)	344.6	(130.4)
Total Other Comprehensive Income (Loss)	(88.6)	(373.0)	166.2
Comprehensive Income	$324.8	$485.1	$1,060.6

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Unum Group and Subsidiaries

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Common Stock			
Balance at Beginning of Year	$36.1	$36.0	$35.9
Common Stock Activity	0.1	0.1	0.1
Retirement of Treasury Stock	(6.0)	—	—
Balance at End of Year	30.2	36.1	36.0
Additional Paid-in Capital			
Balance at Beginning of Year	2,634.1	2,607.7	2,591.1
Common Stock Activity	28.4	26.4	16.6
Retirement of Treasury Stock	(441.3)	—	—
Balance at End of Year	2,221.2	2,634.1	2,607.7
Accumulated Other Comprehensive Income			
Balance at Beginning of Year	255.0	628.0	461.8
Other Comprehensive Income (Loss)	(88.6)	(373.0)	166.2
Balance at End of Year	166.4	255.0	628.0
Retained Earnings			
Balance at Beginning of Year	8,083.2	7,371.6	6,611.0
Net Income	413.4	858.1	894.4
Dividends to Stockholders (per common share: $0.62; $0.55; $0.47)	(159.4)	(146.5)	(133.8)
Retirement of Treasury Stock	(1,004.4)	—	—
Balance at End of Year	7,332.8	8,083.2	7,371.6
Treasury Stock			
Balance at Beginning of Year	(2,349.3)	(2,030.7)	(1,530.1)
Purchases of Treasury Stock	(300.6)	(318.6)	(500.6)
Retirement of Treasury Stock	1,451.7	—	—
Balance at End of Year	(1,198.2)	(2,349.3)	(2,030.7)
Total Stockholders' Equity at End of Year	$8,552.4	$8,659.1	$8,612.6

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Unum Group and Subsidiaries

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Cash Flows from Operating Activities			
Net Income	$413.4	$858.1	$894.4
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities			
Change in Receivables	(21.5)	(196.7)	40.4
Change in Deferred Acquisition Costs	(83.2)	(47.9)	(88.6)
Change in Insurance Reserves and Liabilities	972.2	572.5	508.4
Change in Income Taxes	(44.7)	(49.4)	168.0
Change in Other Accrued Liabilities	105.2	21.2	18.6
Non-cash Components of Net Investment Income	(180.9)	(211.5)	(221.3)
Net Realized Investment Gain	(16.1)	(6.8)	(56.2)
Depreciation	87.9	84.8	84.3
Other, Net	(8.7)	7.2	31.6
Net Cash Provided by Operating Activities	1,223.6	1,031.5	1,379.6
Cash Flows from Investing Activities			
Proceeds from Sales of Fixed Maturity Securities	450.1	1,040.5	595.9
Proceeds from Maturities of Fixed Maturity Securities	1,819.4	2,146.4	2,160.5
Proceeds from Sales and Maturities of Other Investments	235.0	243.4	182.2
Purchase of Fixed Maturity Securities	(2,918.4)	(3,553.6)	(3,512.8)
Purchase of Other Investments	(285.2)	(363.7)	(353.8)
Net Sales (Purchases) of Short-term Investments	(69.3)	551.3	(34.5)
Net Increase (Decrease) in Payables for Collateral on Investments	(3.8)	(378.2)	97.9
Net Purchases of Property and Equipment	(114.5)	(105.5)	(105.4)
Other, Net	0.1	0.2	0.1
Net Cash Used by Investing Activities	(886.6)	(419.2)	(969.9)
Cash Flows from Financing Activities			
Issuance of Long-term Debt	347.2	—	246.4
Long-term Debt Repayments	(186.6)	(116.2)	(70.0)
Cost Related to Early Retirement of Debt	(13.2)	—	—
Issuance of Common Stock	12.3	11.4	4.9
Repurchase of Common Stock	(306.0)	(317.2)	(496.7)
Dividends Paid to Stockholders	(159.4)	(146.5)	(133.8)
Other, Net	(22.9)	(27.0)	0.2
Net Cash Used by Financing Activities	(328.6)	(595.5)	(449.0)
Net Increase (Decrease) in Cash and Bank Deposits	8.4	16.8	(39.3)
Cash and Bank Deposits at Beginning of Year	94.1	77.3	116.6

Cash and Bank Deposits at End of Year	$102.5	$94.1	$77.3

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies

Basis of Presentation: The accompanying consolidated financial statements of Unum Group and its subsidiaries (the Company) have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). Such accounting principles differ from statutory accounting principles (see Note 15). Intercompany transactions have been eliminated.

Description of Business: We are the largest provider of group and individual disability products in the United States and the United Kingdom. We also provide a complementary portfolio of other insurance products, including life insurance, employer- and employee-paid group benefits, and other related services. We market our products primarily to employers interested in providing benefits to their employees.

We have three principal operating business segments: Unum US, Unum UK, and Colonial Life. Our other reporting segments are Closed Block and Corporate. See Note 13 for further discussion of our operating segments.

Use of Estimates: The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

Fixed Maturity Securities: Fixed maturity securities include long-term bonds and redeemable preferred stocks. Fixed maturity securities not bought and held for the purpose of selling in the near term but for which we do not have the positive intent and ability to hold to maturity are classified as available-for-sale and reported at fair value. Changes in the fair value of available-for-sale fixed maturity securities, except for amounts related to other-than-temporary impairment losses recognized in earnings, are reported as a component of other comprehensive income. These amounts are net of income tax and valuation adjustments to deferred acquisition costs and reserves for future policy and contract benefits which would have been recorded had the related unrealized gain or loss on these securities been realized.

Interest income is recorded as part of net investment income when earned, using an effective yield method giving effect to amortization of premium and accretion of discount. Included within fixed maturity securities are mortgage-backed and asset-backed securities. We recognize investment income on these securities using a constant effective yield based on projected prepayments of the underlying loans and the estimated economic life of the securities. Actual prepayment experience is reviewed periodically, and effective yields are recalculated when differences arise between prepayments originally projected and the actual prepayments received and currently projected. The effective yield is recalculated on a retrospective basis, and the adjustment is reflected in net investment income. For fixed maturity securities on which collection of investment income is uncertain, we discontinue the accrual of investment income and recognize investment income when interest and dividends are received. Payment terms specified for fixed maturity securities may include a prepayment penalty for unscheduled payoff of the investment. Prepayment penalties are recognized as investment income when received.

In determining when a decline in fair value below amortized cost of a fixed maturity security is other than temporary, we evaluate available information, both positive and negative, in reaching our conclusions. In particular, we consider the strength of the issuer's balance sheet, its debt obligations and near-term funding requirements, cash flow and liquidity, the profitability of its core businesses, the availability of marketable assets which could be sold to increase liquidity, its industry fundamentals and regulatory environment, and its access to capital markets. Although all

available and applicable factors are considered in our analysis, our expectation of recovering the entire amortized cost basis of the security, whether we intend to sell the security, whether it is more likely than not that we will be required to sell the security before recovery of its amortized cost, and whether the security is current on principal and interest payments are the most critical factors in determining whether impairments are other than temporary. The significance of the decline in value and the length of time during which there has been a significant decline are also important factors, but we generally do not record an impairment loss based solely on these two factors, since often other more relevant factors will impact our evaluation of a security.

If we determine that the decline in value of an investment is other than temporary, the investment is written down to fair value, and an impairment loss is recognized in the current period, either in earnings or in both earnings and other comprehensive income, as applicable. Other-than-temporary impairment losses on fixed maturity securities which we intend to sell or more likely than not will be required to sell before recovery in value are recognized in earnings and equal the entire difference between the security's amortized cost basis and its fair value. For securities which we do not intend to sell and it is not more likely than not that we will be required to sell before recovery in value, other-than-temporary impairment losses recognized in earnings generally represent the difference between the amortized cost of the security and the present value of our best estimate

of cash flows expected to be collected, discounted using the effective interest rate implicit in the security at the date of acquisition. For fixed maturity securities for which we have recognized an other-than-temporary impairment loss through earnings, if through subsequent evaluation there is a significant increase in expected cash flows, the difference between the new amortized cost basis and the cash flows expected to be collected is accreted as net investment income over the remaining life of the investment. See Notes 2 and 3.

Mortgage Loans: Mortgage loans are generally held for investment and are carried at amortized cost less an allowance for probable losses. Interest income is accrued on the principal amount of the loan based on the loan's contractual interest rate. Prepayment penalties are recognized as investment income when received. For mortgage loans on which collection of interest income is uncertain, we discontinue the accrual of interest and recognize it in the period when an interest payment is received. We typically do not resume the accrual of interest on mortgage loans on nonaccrual status until there are significant improvements in the underlying financial condition of the borrower. We consider a loan to be delinquent if full payment is not received in accordance with the contractual terms of the loan.

We evaluate each of our mortgage loans individually for impairment and assign an internal credit quality rating based on a comprehensive rating system used to evaluate the credit risk of the loan. Although all available and applicable factors are considered in our analysis, loan-to-value and debt service coverage ratios are the most critical factors in determining impairment. If we determine that it is probable we will be unable to collect all amounts due under the contractual terms of a mortgage loan, we establish an allowance for credit loss. If we expect to foreclose on the property, the amount of the allowance typically equals the excess carrying value of the mortgage loan over the fair value of the underlying collateral. If we expect to retain the mortgage loan until payoff, the allowance equals the excess carrying value of the mortgage loan over the expected future cash flows of the loan. Additions and reductions to our allowance for credit losses on mortgage loans are reported as a component of net realized investment gains and losses. We do not purchase mortgage loans with existing credit impairments. See Note 3.

Policy Loans: Policy loans are presented at unpaid balances directly related to policyholders. Interest income is accrued on the principal amount of the loan based on the loan's contractual interest rate. Included in policy loans are $3,068.4 million and $3,043.7 million of policy loans ceded to reinsurers at December 31, 2014 and 2013, respectively.

Other Long-term Investments: Other long-term investments are comprised primarily of tax credit partnerships and private equity partnerships.

Tax credit partnerships in which we have invested were formed for the purpose of investing in the construction and rehabilitation of low-income housing. Because the partnerships are structured such that there is no return of principal, the primary sources of investment return from our tax credit partnerships are tax credits and tax benefits derived from passive losses on the investments, both of which may exhibit variability over the life of the investment. These partnerships are accounted for using either the equity or the effective yield method, depending primarily on whether the tax credits are guaranteed through a letter of credit, a tax indemnity agreement, or another similar arrangement. Tax credits received from these partnerships are reported in our consolidated statements of income as either a reduction of state premium taxes, which are a component of other expenses, or a reduction of income tax. For those partnerships accounted for under the equity method, the amortization of the principal amount invested in these partnerships is reported as a component of net investment income. For those partnerships accounted for under the effective yield method, amortization of the principal amount invested is reported as a component of income tax or

other expenses. We will adopt updated accounting guidance for tax credit partnerships, where applicable, effective January 1, 2015. See "Accounting Updates Outstanding" as follows for further discussion.

Our investments in private equity partnerships are passive in nature. The underlying investments held by these partnerships include both equity and debt securities and are accounted for using the equity or cost method, depending on the level of ownership and the degree of our influence over partnership operating and financial policies. For partnerships accounted for under the equity method, our portion of partnership earnings is reported as a component of net investment income in our consolidated statements of income. For those partnerships accounted for under the cost method, we record income received from partnership distributions as either a component of net investment income or net realized investment gain or loss, in accordance with the source of the funds distributed from the partnership. See Notes 2 and 3.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies - Continued

Short-term Investments: Short-term investments are carried at cost. Short-term investments include investments maturing within one year, such as corporate commercial paper and U.S. Treasury bills, bank term deposits, and other cash accounts and cash equivalents earning interest. See Note 2.

Cash and Bank Deposits: Cash and bank deposits include cash on hand and non-interest bearing cash and deposit accounts.

Derivative Financial Instruments: Derivative financial instruments (including certain derivative instruments embedded in other contracts) are recognized as either other long-term investments or other liabilities in our consolidated balance sheets and are reported at fair value. The accounting for a derivative depends on whether it has been designated and qualifies as part of a hedging relationship, and further, on the type of hedging relationship. To qualify for hedge accounting, at the inception of the hedging transaction, we formally document the risk management objective and strategy for undertaking the hedging transaction, as well as the designation of the hedge as either a fair value hedge or a cash flow hedge. Included in this documentation is how the hedging instrument is expected to hedge the designated risk(s) related to specific assets or liabilities on the balance sheet or to specific forecasted transactions as well as a description of the method that will be used to retrospectively and prospectively assess the hedging instrument's effectiveness and the method that will be used to measure ineffectiveness.

A derivative designated as a hedging instrument must be assessed as being highly effective in offsetting the designated risk(s) of the hedged item. Hedge effectiveness is formally assessed at inception and periodically throughout the life of the designated hedging relationship, using qualitative and quantitative methods. Qualitative methods include comparison of critical terms of the derivative to the hedged item. Quantitative methods include regression or other statistical analysis of changes in fair value or cash flows associated with the hedge relationship.

Changes in the fair value of a derivative designated as a fair value hedge, including amounts measured as ineffectiveness, and changes in the fair value of the hedged item attributable to the risk being hedged are recognized in earnings as a component of net realized investment gain or loss during the period of change in fair value. The gain or loss on the termination of a fair value hedge is recognized in earnings as a component of net realized investment gain or loss during the period in which the termination occurs. When interest rate swaps are used in hedge accounting relationships, periodic settlements are recorded in the same income statement line as the related settlements of the hedged items.

To the extent it is effective, changes in the fair value of a derivative designated as a cash flow hedge are reported in other comprehensive income and reclassified into earnings and reported on the same income statement line item as the hedged item and in the same period or periods during which the hedged item affects earnings. The ineffective portion of the hedge, if any, is recognized in earnings as a component of net realized investment gain or loss during the period of change in fair value. The gain or loss on the termination of an effective cash flow hedge is reported in other comprehensive income and reclassified into earnings and reported on the same income statement line item as the hedged item and in the same period or periods during which the hedged item affects earnings.

Gains or losses on the termination of ineffective fair value or cash flow hedges are reported in earnings as a component of net realized investment gain or loss. In the event a hedged item is disposed of or the anticipated transaction being hedged is no longer likely to occur, we will terminate the related derivative and recognize the gain or loss on termination in current earnings as a component of net realized investment gain or loss. In the event a hedged

item is disposed of subsequent to the termination of the hedging transaction, we reclassify any remaining gain or loss on the cash flow hedge out of accumulated other comprehensive income into earnings as a component of the same income statement line item wherein we report the gain or loss on disposition of the hedged item.

For a derivative not designated as a hedging instrument, changes in the fair value of the derivative, together with the payment of periodic fees, if applicable, are recognized in earnings as a component of net realized investment gain or loss during the period of change in fair value.

Cash flow activity from the settlement of derivative contracts is reported in the consolidated statements of cash flows as a component of proceeds from sales and maturities of other investments.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies - Continued

In our consolidated balance sheets, we do not offset fair value amounts recognized for derivatives executed with the same counterparty under a master netting agreement and fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral arising from those master netting agreements. See Notes 2, 3 and 4.

Fair Value Measurement: Certain assets and liabilities are reported at fair value in our consolidated balance sheets and in our notes to our consolidated financial statements. We define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Therefore, fair value represents an exit price, not an entry price. The exit price objective applies regardless of our intent and/or ability to sell the asset or transfer the liability at the measurement date. Assets or liabilities with readily available actively quoted prices or for which fair value can be measured from actively quoted prices in active markets generally have more pricing observability and less judgment utilized in measuring fair value. When actively quoted prices are not available, fair values are based on quoted prices in markets that are not active, quoted prices for similar but not identical assets or liabilities, or other observable inputs. If observable inputs are not available, unobservable inputs and/or adjustments to observable inputs requiring management judgment are used to determine fair value. We categorize our assets and liabilities measured at estimated fair value into a three-level hierarchy, based on the significance of the inputs. The fair value hierarchy gives the highest priority to inputs which are unadjusted and represent quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). See Note 2.

Realized Investment Gains and Losses: Realized investment gains and losses are reported as a component of revenue in the consolidated statements of income and are based upon specific identification of the investments sold. See Note 3.

Deferred Acquisition Costs: Incremental direct costs associated with the successful acquisition of new or renewal insurance contracts have been deferred. Such costs include commissions, other agency compensation, certain selection and policy issue expenses, and certain field expenses. Acquisition costs that do not vary with the production of new business, such as commissions on group products which are generally level throughout the life of the policy, are excluded from deferral. Deferred acquisition costs are subject to recoverability testing at the time of policy issue and loss recognition testing in subsequent years.

Deferred acquisition costs related to non interest-sensitive policies are amortized in proportion to the premium income we expect to receive over the life of the policies. Deferred acquisition costs related to interest-sensitive policies are amortized over the lives of the policies in relation to the present value of estimated gross profits from surrender charges, mortality margins, investment returns, and expense margins. Deviations from projections result in a change to the rate of amortization in the period during which such events occur. Generally, the amortization periods for these policies approximate the estimated lives of the policies.

For certain products, policyholders can elect to modify product benefits, features, rights, or coverages by exchanging a contract for a new contract or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. These transactions are known as internal replacement transactions. Internal replacement transactions wherein the modification does not substantially change the policy are accounted for as continuations of the replaced contracts. Unamortized deferred acquisition costs from the original policy continue to be amortized over the expected life of the new policy, and the costs of replacing the policy are accounted for as policy maintenance costs and expensed as incurred. Internal replacement transactions, principally on group contracts, that result in a policy that

is substantially changed are accounted for as an extinguishment of the original policy and the issuance of a new policy. Unamortized deferred acquisition costs on the original policy that was replaced are immediately expensed, and the costs of acquiring the new policy are capitalized and amortized in accordance with our accounting policies for deferred acquisition costs.

Loss recognition is performed on an annual basis, or more frequently if appropriate, using best estimate assumptions as to future experience as of the date of the test. Insurance contracts are grouped for each major product line within a segment when we perform the loss recognition tests. If loss recognition testing indicates that deferred acquisition costs are not recoverable, the deficiency is charged to expense.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies - Continued

Goodwill: Goodwill is the excess of the amount paid to acquire a business over the fair value of the net assets acquired. We review the carrying amount of goodwill for impairment on an annual basis, or more frequently if events or changes in circumstances indicate that the carrying amount might not be recoverable. Goodwill impairment testing compares the fair value of a reporting unit with its carrying amount, including goodwill. The fair values of the reporting units are determined using discounted cash flow models. The critical estimates necessary in determining fair value are projected earnings and the discount rate. We set our discount rate assumption based on an expected risk adjusted cost of capital. If the fair value of the reporting unit to which the goodwill relates is less than the carrying amount of the unamortized goodwill, the carrying amount is reduced with a corresponding charge to expense.

Property and Equipment: Property and equipment is reported at cost less accumulated depreciation, which is calculated on the straight-line method over the estimated useful life. The accumulated depreciation for property and equipment was $823.3 million and $760.8 million as of December 31, 2014 and 2013, respectively.

Value of Business Acquired: Value of business acquired represents the present value of future profits recorded in connection with the acquisition of a block of insurance policies. The asset is amortized based upon expected future premium income for non interest-sensitive insurance policies and estimated future gross profits from surrender charges, mortality margins, investment returns, and expense margins for interest-sensitive insurance policies. The value of business acquired, which is included in other assets in our consolidated balance sheets, was $15.2 million and $19.0 million at December 31, 2014 and 2013, respectively. The accumulated amortization for value of business acquired was $134.7 million and $138.2 million as of December 31, 2014 and 2013, respectively.

The amortization of value of business acquired, which is included in other expenses in the consolidated statements of income, was $3.5 million, $4.5 million, and $7.5 million for the years ended December 31, 2014, 2013, and 2012, respectively. We periodically review the carrying amount of value of business acquired using the same methods used to evaluate deferred acquisition costs.

Policy and Contract Benefits: Policy and contract benefits represent amounts paid and expected to be paid based on reported losses and estimates of incurred but not reported losses for non interest-sensitive life and accident and health products. For interest-sensitive products, benefits are the amounts paid and expected to be paid on insured claims in excess of the policyholders' policy fund balances.

Reserves for Policy and Contract Benefits: Policy reserves represent future policy and contract benefits for claims not yet incurred. Policy reserves for non interest-sensitive life and accident and health products are determined using the net level premium method. The reserves are calculated based upon assumptions as to interest, persistency, morbidity, and mortality that were appropriate at the date of issue. Discount rate assumptions are based on actual and expected net investment returns. Persistency assumptions are based on our actual historical experience adjusted for future expectations. Claim incidence and claim resolution rate assumptions related to morbidity and mortality are based on actual experience or industry standards adjusted as appropriate to reflect our actual experience and future expectations. The assumptions vary by plan, year of issue, and policy duration and include a provision for adverse deviation.

Policy reserves for group single premium annuities are developed on a net single premium method. The reserves are calculated based on assumptions as to interest, mortality, and retirement that were appropriate at the date of issue. Mortality assumptions are based upon industry standards adjusted as appropriate to reflect our actual experience and future expectations. The assumptions vary by year of issue.

Policy reserves for interest-sensitive products are principally policyholder account values.

Policy reserves require ongoing loss recognition testing. We perform loss recognition tests on our policy reserves annually, or more frequently if appropriate, using best estimate assumptions as of the date of the test, without a provision for adverse deviation. We group the policy reserves for each major product line within a segment when we perform the loss recognition tests. If the policy reserves determined using these best estimate assumptions are higher than our existing policy reserves net of any deferred acquisition cost balance, the existing policy reserves are increased or deferred acquisition costs are reduced to immediately recognize the deficiency. This becomes the new basis for policy reserves going forward, subject to future loss recognition testing.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies - Continued

Claim reserves represent future policy and contract benefits for claims that have been incurred or are estimated to have been incurred but not yet reported to us. Our claim reserves relate primarily to disability policies and are calculated based on assumptions as to interest and claim resolution rates that are currently appropriate. Claim resolution rate assumptions are based on our actual experience. The interest rate assumptions used for discounting claim reserves are based on projected portfolio yield rates, after consideration for defaults and investment expenses, for the assets supporting the liabilities for the various product lines. Unlike policy reserves for which assumptions are generally established and locked in at the time of policy issuance, claim reserves are subject to revision as current claim experience and projections of future factors affecting claim experience change. See Note 6.

Policyholders' Funds: Policyholders' funds represent customer deposits plus interest credited at contract rates. We control interest rate risk by investing in quality assets which have an aggregate duration that closely matches the expected duration of the liabilities.

Income Tax: Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial statement purposes and the amounts used for income tax purposes. Deferred taxes have been measured using enacted statutory income tax rates and laws that are currently in effect. We record deferred tax assets for tax positions taken in the U.S. and other tax jurisdictions based on our assessment of whether a position is more likely than not to be sustained upon examination based solely on its technical merits. A valuation allowance is established for deferred tax assets when it is more likely than not that an amount will not be realized. See Note 7.

Short-term and Long-term Debt: Debt is generally carried at the unpaid principal balance, net of unamortized discount or premium. Short-term debt consists of debt due within the next twelve months, including that portion of debt otherwise classified as long-term. Original issue discount or premium as well as debt issue costs are recognized as a component of interest expense over the period the debt is expected to be outstanding. The carrying amount of long-term debt that is part of a fair value hedge program includes an adjustment to reflect the effect of the change in fair value attributable to the risk being hedged. Net interest settlements for fair value hedges on our long-term debt are recognized as a component of interest expense. See Note 8.

Treasury Stock and Retirement of Common Stock: Treasury stock is reflected as a reduction of stockholders' equity at cost. When shares are retired, the par value is removed from common stock, and the excess of the repurchase price over par is allocated between additional paid-in capital and retained earnings. See Note 10.

Revenue Recognition: Our non interest-sensitive life and accident and health products are long-duration contracts, and premium income is recognized as revenue when due from policyholders. If the contracts are experience rated, the estimated ultimate premium is recognized as revenue over the period of the contract. The estimated ultimate premium, which is revised to reflect current experience, is based on estimated claim costs, expenses, and profit margins.

For interest-sensitive products, the amounts collected from policyholders are considered deposits, and only the deductions during the period for cost of insurance, policy administration, and surrenders are included in revenue. Policyholders' funds represent funds deposited by contract holders and are not included in revenue.

Fees from our administrative-services only and family medical leave products are reported as other income when services are rendered.

Reinsurance: We routinely enter into reinsurance agreements with other insurance companies to spread risk and thereby limit losses from large exposures. For each of our reinsurance agreements, we determine if the agreement provides indemnification against loss or liability relating to insurance risk in accordance with applicable accounting standards. If we determine that a reinsurance agreement does not expose the reinsurer to a reasonable possibility of a significant loss from insurance risk, we record the agreement using the deposit method of accounting.

Reinsurance activity is accounted for on a basis consistent with the terms of the reinsurance contracts and the accounting used for the original policies issued. Premium income and benefits and change in reserves for future benefits are presented in our consolidated statements of income net of reinsurance ceded. Ceded liabilities for policy and contract benefits, future policy and contract benefits, and unearned premiums are reported on a gross basis in our consolidated balance sheets, as are ceded policy

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies - Continued

loans. Our reinsurance recoverable includes the balances due from reinsurers under the terms of the reinsurance agreements for these ceded balances as well as settlement amounts currently due.

Where applicable, gains or losses on reinsurance transactions are deferred and amortized into earnings based upon expected future premium income for non interest-sensitive insurance policies and estimated future gross profits for interest-sensitive insurance policies. The deferred gain on reinsurance included in other liabilities in our consolidated balance sheets at December 31, 2014 and 2013 was $41.7 million and $53.6 million, respectively.

Under ceded reinsurance agreements wherein we are not relieved of our legal liability to our policyholders, if the assuming reinsurer is unable to meet its obligations, we remain contingently liable. We evaluate the financial condition of reinsurers and monitor concentration of credit risk to minimize this exposure. We may also require assets in trust, letters of credit, or other acceptable collateral to support our reinsurance recoverable balances. In the event that reinsurers do not meet their obligations to us under the terms of the reinsurance agreements, certain amounts reported in our reinsurance recoverable could become uncollectible, in which case the reinsurance recoverable balances are stated net of allowances for uncollectible reinsurance. See Note 12.

Premium Tax Expense: Premium tax expense is included in other expenses in the consolidated statements of income. For the years ended December 31, 2014, 2013, and 2012, premium tax expense was $139.2 million, $137.0 million, and $136.0 million, respectively.

Stock-Based Compensation: The cost of stock-based compensation is generally measured based on the grant-date fair value of the award. The Black-Scholes options valuation model is used for estimating the fair value of stock options, and the Monte-Carlo valuation model is used for estimating the fair value of performance share units. Restricted stock units are valued based on the fair value of common stock at the grant date, and cash-settled awards are measured each reporting period based on the current stock price. Stock-based awards are expensed over the requisite service period, or for performance share units over the requisite service period, or remaining service period, if and when it becomes probable that the performance conditions will be satisfied, with an offsetting increase to additional paid-in capital in stockholders' equity. See Note 11.

Earnings Per Share: We compute basic earnings per share by dividing net income by the weighted average number of common shares outstanding for the period. Earnings per share assuming dilution is computed by dividing net income by the weighted average number of shares outstanding for the period plus the shares representing the dilutive effect of stock-based awards. In computing earnings per share assuming dilution, only potential common shares resulting from stock-based awards that are dilutive (those that reduce earnings per share) are included. We use the treasury stock method to account for the effect of outstanding stock options and nonvested stock awards on the computation of earnings per share assuming dilution. See Note 10.

Translation of Foreign Currency: Revenues and expenses of our foreign operations are translated at average exchange rates. Assets and liabilities are translated at the rate of exchange on the balance sheet dates. The translation gain or loss is generally reported in accumulated other comprehensive income, net of deferred tax. We do not provide for deferred taxes to the extent unremitted foreign earnings are deemed permanently invested.

Accounting for Participating Individual Life Insurance: Participating policies issued by one of our subsidiaries prior to its 1986 conversion from a mutual to a stock life insurance company will remain participating as long as the policies

remain in-force. A Participation Fund Account (PFA) was established for the benefit of all such individual participating life and annuity policies and contracts. The assets of the PFA provide for the benefit, dividend, and certain expense obligations of the participating individual life insurance policies and annuity contracts. The assets of the PFA were $358.6 million and $339.2 million at December 31, 2014 and 2013, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 1 - Significant Accounting Policies - Continued

Accounting Updates Outstanding:

Accounting Standards Codification (ASC)	Description	Date of Adoption	Effect on Financial Statements
ASC 606 "Revenue from Contracts with Customers"	This update supersedes virtually all existing guidance regarding the recognition of revenue from customers. Specifically excluded from the scope of this update are insurance contracts, although our fee-based service products are included within the scope. The core principal of this guidance is that revenue recognition should depict the transfer of goods or services to customers in an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services. The guidance is to be applied retrospectively.	January 1, 2017	The adoption of this update will not have a material effect on our financial position or results of operations.
ASC 860 "Transfers and Servicing"	This update changes the accounting for repurchase-to-maturity transactions and linked repurchase financings to secured borrowing accounting, which is consistent with the accounting for other repurchase agreements. The update also requires disclosures for repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions. The guidance is to be applied retrospectively for transactions outstanding on the effective date of the update.	January 1, 2015, except for certain disclosures, which will be effective April 1, 2015.	The adoption of this update will expand our disclosures but will not impact our financial position or results of operations.
ASC 323 "Investments - Equity Method and Joint Ventures"	This update permits entities to make an accounting policy election to account for investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). Additional disclosures concerning investments in qualified affordable housing projects are also required. We have elected to adopt this guidance, which will be applied retrospectively.	January 1, 2015	See table as follows.

Our retrospective adoption of the update to ASC 323 as of January 1, 2015 will result in a cumulative effect decrease in stockholders' equity as of January 1, 2015, 2014, and 2013 of approximately $30 million, $19 million, and $8 million, respectively. Our net income and earnings per share assuming dilution will be impacted as follows:

(in millions, except per share data)	Year Ended December 31					
	2014		2013		2012	
		per share		per share		per share
Net Income, Before Adoption	$413.4	$1.61	$858.1	$3.23	$894.4	$3.17
After-tax Impact of Adoption	(11.3)	(0.04)	(11.1)	(0.04)	(6.3)	(0.02)

Net Income, After Adoption	$402.1	$1.57	$847.0	$3.19	$888.1	$3.15

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments

Presented as follows are the carrying amounts and fair values of financial instruments. The carrying values of financial instruments such as short-term investments, cash and bank deposits, accounts and premiums receivable, accrued investment income, and securities lending agreements approximate fair value due to the short-term nature of the instruments. As such, these financial instruments are not included in the following chart.

	December 31, 2014		December 31, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(in millions of dollars)			
Assets				
Fixed Maturity Securities	$45,064.9	$45,064.9	$42,344.4	$42,344.4
Mortgage Loans	1,856.6	2,024.2	1,815.1	1,980.2
Policy Loans	3,306.6	3,407.6	3,276.0	3,339.6
Other Long-term Investments				
Derivatives	28.0	28.0	10.8	10.8
Equity Securities	12.5	12.5	16.4	16.4
Miscellaneous Long-term Investments	485.5	485.5	475.2	475.2
Liabilities				
Policyholders' Funds				
Deferred Annuity Products	$621.4	$621.4	$631.5	$631.5
Supplementary Contracts without Life Contingencies	600.4	600.4	563.1	563.1
Short-term Debt	151.9	158.9	—	—
Long-term Debt	2,628.7	2,912.6	2,612.0	2,824.4
Other Liabilities				
Derivatives	92.9	92.9	135.6	135.6
Embedded Derivative in Modified Coinsurance Arrangement	49.9	49.9	53.2	53.2
Unfunded Commitments to Investment Partnerships	12.8	12.8	27.2	27.2

The methods and assumptions used to estimate fair values of financial instruments are discussed as follows.

Fair Value Measurements for Financial Instruments Not Carried at Fair Value

Mortgage Loans: Fair values are estimated using discounted cash flow analyses and interest rates currently being offered for similar loans to borrowers with similar credit ratings and maturities. Loans with similar characteristics are aggregated for purposes of the calculations. These financial instruments are assigned a Level 2 within the fair value hierarchy.

Policy Loans: Fair values for policy loans, net of reinsurance ceded, are estimated using discounted cash flow analyses and interest rates currently being offered to policyholders with similar policies. Carrying amounts for ceded policy loans, which equal $3,068.4 million and $3,043.7 million as of December 31, 2014 and 2013, respectively, approximate fair value and are reported on a gross basis in our consolidated balance sheets. A change in interest rates for ceded policy loans will not impact our financial position because the benefits and risks are fully ceded to reinsuring counterparties. These financial instruments are assigned a Level 3 within the fair value hierarchy.

Miscellaneous Long-term Investments: Carrying amounts for tax credit partnerships equal the unamortized balance of our contractual commitments and approximate fair value. Fair values for private equity partnerships are primarily derived from net asset values provided by the general partner in the partnerships' financial statements. Our private equity partnerships represent funds that are primarily invested in railcar leasing, the financial services industry, mezzanine debt, and bank loans. Distributions received from the funds arise from income generated by the underlying investments as well as the liquidation of the underlying investments. As of December 31, 2014, we estimate that the underlying assets of the funds will be liquidated over the next one to thirteen years. These financial instruments are assigned a Level 3 within the fair value hierarchy.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

Policyholders' Funds: Policyholders' funds are comprised primarily of deferred annuity products and supplementary contracts without life contingencies and represent customer deposits plus interest credited at contract rates. Carrying amounts approximate fair value. These financial instruments are assigned a Level 3 within the fair value hierarchy.

Fair values for insurance contracts other than investment contracts are not required to be disclosed. However, the fair values of liabilities under all insurance contracts are taken into consideration in our overall management of interest rate risk, which seeks to minimize exposure to changing interest rates through the matching of investment maturities with amounts due under insurance contracts.

Short-term Debt: Fair values for short-term debt were determined based on prices from independent pricing services that generally use observable inputs for securities or comparable securities in active markets in their valuation techniques. These financial instruments are assigned a Level 2.

Long-term Debt: Fair values for long-term debt are obtained from independent pricing services or discounted cash flow analyses based on current incremental borrowing rates for similar types of borrowing arrangements. Debt instruments which are valued using active trades from independent pricing services for which there was current market activity in that specific debt instrument have fair values of $849.7 million and $1,329.2 million as of December 31, 2014 and 2013, respectively, and are assigned a Level 1 within the fair value hierarchy. Debt instruments which are valued based on prices from pricing services that generally use observable inputs for securities or comparable securities in active markets in their valuation techniques have fair values of $2,062.9 million and $1,495.2 million as of December 31, 2014 and 2013, respectively, and are assigned a Level 2.

Unfunded Commitments to Investment Partnerships: Unfunded equity commitments represent legally binding amounts that we have committed to certain investment partnerships subject to the partnerships meeting specified conditions. When these conditions are met, we are obligated to invest these amounts in the partnerships. Carrying amounts approximate fair value. These financial instruments are assigned a Level 2 within the fair value hierarchy.

Fair Value Measurements for Financial Instruments Carried at Fair Value

We report fixed maturity securities, derivative financial instruments, and equity securities at fair value in our consolidated balance sheets. The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of pricing observability. Financial instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices in active markets generally have more pricing observability and less judgment utilized in measuring fair value. An active market for a financial instrument is a market in which transactions for an asset or a similar asset occur with sufficient frequency and volume to provide pricing information on an ongoing basis. A quoted price in an active market provides the most reliable evidence of fair value and should be used to measure fair value whenever available. Conversely, financial instruments rarely traded or not quoted have less observability and are measured at fair value using valuation techniques that require more judgment. Pricing observability is generally impacted by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction, and overall market conditions.

Valuation techniques used for assets and liabilities accounted for at fair value are generally categorized into three types. The market approach uses prices and other relevant information from market transactions involving identical or comparable assets or liabilities. The income approach converts future amounts, such as cash flows or earnings, to a

single present amount, or a discounted amount. The cost approach is based upon the amount that currently would be required to replace the service capacity of an asset, or the current replacement cost.

We use valuation techniques that are appropriate in the circumstances and for which sufficient data are available that can be obtained without undue cost and effort. In some cases, a single valuation technique will be appropriate (for example, when valuing an asset or liability using quoted prices in an active market for identical assets or liabilities). In other cases, multiple valuation techniques will be appropriate. If we use multiple valuation techniques to measure fair value, we evaluate and weigh the results, as appropriate, considering the reasonableness of the range indicated by those results. A fair value measurement is the point within that range that is most representative of fair value in the circumstances.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

The selection of the valuation method(s) to apply considers the definition of an exit price and depends on the nature of the asset or liability being valued. For assets and liabilities accounted for at fair value, we generally use valuation techniques consistent with the market approach, and to a lesser extent, the income approach. We believe the market approach valuation technique provides more observable data than the income approach, considering the type of investments we hold. Our fair value measurements could differ significantly based on the valuation technique and available inputs. When using a pricing service, we obtain the vendor's pricing documentation to ensure we understand their methodologies. We periodically review and approve the selection of our pricing vendors to ensure we are in agreement with their current methodologies. When markets are less active, brokers may rely more on models with inputs based on the information available only to the broker. Our internal investment management professionals, which include portfolio managers and analysts, monitor securities priced by brokers and evaluate their prices for reasonableness based on benchmarking to available primary and secondary market information. In weighing a broker quote as an input to fair value, we place less reliance on quotes that do not reflect the result of market transactions. We also consider the nature of the quote, particularly whether the quote is a binding offer. If prices in an inactive market do not reflect current prices for the same or similar assets, adjustments may be necessary to arrive at fair value. When relevant market data is unavailable, which may be the case during periods of market uncertainty, the income approach can, in suitable circumstances, provide a more appropriate fair value. During 2014, we have applied valuation techniques on a consistent basis to similar assets and liabilities and consistent with those techniques used at year end 2013.

We use observable and unobservable inputs in measuring the fair value of our financial instruments. Inputs that may be used include the following:

- Broker market maker prices and price levels
- Trade Reporting and Compliance Engine (TRACE) pricing
- Prices obtained from external pricing services
- Benchmark yields (Treasury and interest rate swap curves)
- Transactional data for new issuance and secondary trades
- Security cash flows and structures
- Recent issuance/supply
- Sector and issuer level spreads
- Security credit ratings/maturity/capital structure/optionality
- Corporate actions
- Underlying collateral
- Prepayment speeds/loan performance/delinquencies/weighted average life/seasoning
- Public covenants
- Comparative bond analysis
- Derivative spreads
- Relevant reports issued by analysts and rating agencies
- Audited financial statements

The management of our investment portfolio includes establishing pricing policy and reviewing the reasonableness of sources and inputs used in developing pricing. We review all prices obtained to ensure they are consistent with a variety of observable market inputs and to verify the validity of a security's price. In the event we receive a vendor's market price that does not appear reasonable based on our market analysis, we may challenge the price and request further information about the assumptions and methodologies used by the vendor to price the security. We may

change the vendor price based on a better data source such as an actual trade. We also review all price changes from the prior month which fall outside a predetermined corridor. The overall valuation process for determining fair values may include adjustments to valuations obtained from our pricing sources when they do not represent a valid exit price. These adjustments may be made when, in our judgment and considering our knowledge of the financial conditions and industry in which the issuer operates, certain features of the financial instrument require that an adjustment be made to the value originally obtained from our pricing sources. These features may include the complexity of the financial instrument, the market in which the financial instrument is traded, counterparty credit risk, credit structure, concentration, or liquidity. Additionally, an adjustment to the price derived from a model typically reflects our judgment of the inputs that other participants in the market for the financial instrument being measured at fair value would consider in pricing that same financial instrument. In the event an asset is sold, we test the validity of the fair value determined by our valuation techniques by comparing the selling price to the fair value determined for the asset in the immediately preceding month end reporting period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

The parameters and inputs used to validate a price on a security may be adjusted for assumptions about risk and current market conditions on a quarter to quarter basis, as certain features may be more significant drivers of valuation at the time of pricing. Changes to inputs in valuations are not changes to valuation methodologies; rather, the inputs are modified to reflect direct or indirect impacts on asset classes from changes in market conditions.

Fair values for derivatives other than embedded derivatives in modified coinsurance arrangements are based on market quotes or pricing models and represent the net amount of cash we would have paid or received if the contracts had been settled or closed as of the last day of the period. We analyze credit default swap spreads relative to the average credit spread embedded within the LIBOR-setting syndicate in determining the effect of credit risk on our derivatives' fair values. If net counterparty credit risk for a derivative asset is determined to be material and is not adequately reflected in the LIBOR-based fair value obtained from our pricing sources, we adjust the valuations obtained from our pricing sources. For purposes of valuing net counterparty risk, we measure the fair value of a group of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position or transfer a net short position for a particular risk exposure in an orderly transaction between market participants at the measurement date under current market conditions. In regard to our own credit risk component, we adjust the valuation of derivative liabilities wherein the counterparty is exposed to our credit risk when the LIBOR-based valuation of our derivatives obtained from pricing sources does not effectively include an adequate credit component for our own credit risk.
Fair values for our embedded derivative in a modified coinsurance arrangement are estimated using internal pricing models and represent the hypothetical value of the duration mismatch of assets and liabilities, interest rate risk, and third party credit risk embedded in the modified coinsurance arrangement.

Certain of our investments do not have readily determinable market prices and/or observable inputs or may at times be affected by the lack of market liquidity. For these securities, we use internally prepared valuations combining matrix pricing with vendor purchased software programs, including valuations based on estimates of future profitability, to estimate the fair value. Additionally, we may obtain prices from independent third-party brokers to aid in establishing valuations for certain of these securities. Key assumptions used by us to determine fair value for these securities include risk free interest rates, risk premiums, performance of underlying collateral (if any), and other factors involving significant assumptions which may or may not reflect those of an active market.

At December 31, 2014, approximately 6.6 percent of our fixed maturity securities were valued using active trades from TRACE pricing or broker market maker prices for which there was current market activity in that specific security (comparable to receiving one binding quote). The prices obtained were not adjusted, and the assets were classified as Level 1, the highest category of the three-level fair value hierarchy classification wherein inputs are unadjusted and represent quoted prices in active markets for identical assets or liabilities.

The remaining 93.4 percent of our fixed maturity securities were valued based on non-binding quotes or other observable and unobservable inputs, as discussed below.

- Approximately 78.1 percent of our fixed maturity securities were valued based on prices from pricing services that generally use observable inputs such as prices for securities or comparable securities in active markets in their valuation techniques. These assets were classified as Level 2. Level 2 assets or liabilities are those valued using inputs (other than prices included in Level 1) that are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life.

- Approximately 3.5 percent of our fixed maturity securities were valued based on one or more non-binding broker quotes, if validated by observable market data, or on TRACE prices for identical or similar assets absent current market activity. When only one price is available, it is used if observable inputs and analysis confirms that it is appropriate. These assets, for which we were able to validate the price using other observable market data, were classified as Level 2.

- Approximately 11.8 percent of our fixed maturity securities were valued based on prices of comparable securities, matrix pricing, market models, and/or internal models or were valued based on non-binding quotes with no other observable market data. These assets were classified as either Level 2 or Level 3, with the categorization dependent on whether there was other observable market data. Level 3 is the lowest category of the fair value hierarchy and reflects

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

the judgment of management regarding what market participants would use in pricing assets or liabilities at the measurement date. Financial assets and liabilities categorized as Level 3 are generally those that are valued using unobservable inputs to extrapolate an estimated fair value.

We consider transactions in inactive or disorderly markets to be less representative of fair value. We use all available observable inputs when measuring fair value, but when significant other unobservable inputs and adjustments are necessary, we classify these assets or liabilities as Level 3.

In the following charts, prior year amounts have been reclassified, where applicable, between public utilities and all other corporate bonds to conform to the current year categorization of certain securities.

Fair value measurements by input level for financial instruments carried at fair value are as follows:

	December 31, 2014			
	Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(in millions of dollars)			
Assets				
Fixed Maturity Securities				
United States Government and Government Agencies and Authorities	$297.5	$941.0	$—	$1,238.5
States, Municipalities, and Political Subdivisions	—	1,981.4	140.1	2,121.5
Foreign Governments	—	1,238.1	69.3	1,307.4
Public Utilities	106.2	8,129.4	315.0	8,550.6
Mortgage/Asset-Backed Securities	—	2,431.8	—	2,431.8
All Other Corporate Bonds	2,556.6	25,383.3	1,425.3	29,365.2
Redeemable Preferred Stocks	—	25.0	24.9	49.9
Total Fixed Maturity Securities	2,960.3	40,130.0	1,974.6	45,064.9
Other Long-term Investments				
Derivatives				
Interest Rate Swaps	—	5.7	—	5.7
Foreign Exchange Contracts	—	22.3	—	22.3
Total Derivatives	—	28.0	—	28.0
Equity Securities	—	11.1	1.4	12.5
Liabilities				
Other Liabilities				
Derivatives				
Interest Rate Swaps	$—	$20.8	$—	$20.8
Foreign Exchange Contracts	—	70.9	—	70.9
Credit Default Swaps	—	1.2	—	1.2
	—	—	49.9	49.9

Embedded Derivative in Modified Coinsurance Arrangement				
Total Derivatives	—	92.9	49.9	142.8

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

	December 31, 2013 Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(in millions of dollars)			
Assets				
Fixed Maturity Securities				
United States Government and Government Agencies and Authorities	$144.5	$1,051.6	$—	$1,196.1
States, Municipalities, and Political Subdivisions	—	1,608.1	175.1	1,783.2
Foreign Governments	—	1,294.7	78.5	1,373.2
Public Utilities	246.0	7,611.9	139.3	7,997.2
Mortgage/Asset-Backed Securities	—	2,038.8	0.5	2,039.3
All Other Corporate Bonds	2,132.8	23,861.6	1,923.3	27,917.7
Redeemable Preferred Stocks	—	13.9	23.8	37.7
Total Fixed Maturity Securities	2,523.3	37,480.6	2,340.5	42,344.4
Other Long-term Investments				
Derivatives				
Interest Rate Swaps	—	9.2	—	9.2
Foreign Exchange Contracts	—	1.6	—	1.6
Total Derivatives	—	10.8	—	10.8
Equity Securities	—	11.8	4.6	16.4
Liabilities				
Other Liabilities				
Derivatives				
Interest Rate Swaps	$—	$35.0	$—	$35.0
Foreign Exchange Contracts	—	98.7	—	98.7
Credit Default Swaps	—	1.9	—	1.9
Embedded Derivative in Modified Coinsurance Arrangement	—	—	53.2	53.2
Total Derivatives	—	135.6	53.2	188.8

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

Transfers of assets between Level 1 and Level 2 are as follows:

	Year Ended December 31			
	2014		2013	
	Transfers into			
	Level 1 from Level 2	Level 2 from Level 1	Level 1 from Level 2	Level 2 from Level 1
	(in millions of dollars)			
Fixed Maturity Securities				
United States Government and Government Agencies and Authorities	$163.2	$—	$62.2	$—
States, Municipalities, and Political Subdivisions	—	—	—	53.0
Public Utilities	81.8	253.4	248.4	20.8
All Other Corporate Bonds	1,592.1	1,598.3	1,296.5	1,117.9
Total Fixed Maturity Securities	$1,837.1	$1,851.7	$1,607.1	$1,191.7

Transfers between Level 1 and Level 2 occurred due to the change in availability of either a TRACE or broker market maker price. Depending on current market conditions, the availability of these Level 1 prices can vary from period to period. For fair value measurements of financial instruments that were transferred either into or out of Level 1 or 2, we reflect the transfers using the fair value at the beginning of the period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

Changes in assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) are as follows:

	Year Ended December 31, 2014							
		Total Realized and Unrealized Investment Gains (Losses) Included in				Level 3 Transfers		
	Beginning of Year	Earnings	Other Comprehensive Income or Loss	Purchases	Sales	Into	Out of	End of Year
	(in millions of dollars)							
Fixed Maturity Securities								
States, Municipalities, and Political Subdivisions	$175.1	$—	$21.0	$—	$(1.4)	$—	$(54.6)	$140.1
Foreign Governments	78.5	1.1	0.8	—	(11.1)	—	—	69.3
Public Utilities	139.3	—	6.9	—	(0.8)	199.9	(30.3)	315.0
Mortgage/Asset-Backed Securities	0.5	(0.2)	0.3	—	(0.6)	—	—	—
All Other Corporate Bonds	1,923.3	0.7	44.8	91.1	(147.7)	626.9	(1,113.8)	1,425.3
Redeemable Preferred Stocks	23.8	—	1.1	—	—	—	—	24.9
Total Fixed Maturity Securities	2,340.5	1.6	74.9	91.1	(161.6)	826.8	(1,198.7)	1,974.6
Equity Securities	4.6	10.5	(0.2)	—	(13.5)	—	—	1.4
Embedded Derivative in Modified Coinsurance Arrangement	(53.2)	3.3	—	—	—	—	—	(49.9)

	Year Ended December 31, 2013							
		Total Realized and Unrealized Investment Gains (Losses) Included in				Level 3 Transfers		
	Beginning of Year	Earnings	Other Comprehensive Income or Loss	Purchases	Sales	Into	Out of	End of Year
	(in millions of dollars)							
Fixed Maturity Securities								
States, Municipalities, and Political Subdivisions	$128.7	$—	$(13.1)	$—	$(1.0)	$60.5	$—	$175.1
Foreign Governments	82.1	—	(3.6)	—	—	—	—	78.5
Public Utilities	226.4	—	(1.1)	—	(3.1)	101.9	(184.8)	139.3
	0.5	—	0.1	—	(0.1)	—	—	0.5

Mortgage/Asset-Backed Securities								
All Other Corporate Bonds	1,525.8	1.1	(156.8)	186.7	(122.0)	1,511.9	(1,023.4)	1,923.3
Redeemable Preferred Stocks	24.8	—	(1.0)	—	—	—	—	23.8
Total Fixed Maturity Securities	1,988.3	1.1	(175.5)	186.7	(126.2)	1,674.3	(1,208.2)	2,340.5
Equity Securities	4.3	—	0.3	—	—	—	—	4.6
Embedded Derivative in Modified Coinsurance Arrangement	(83.9)	30.7	—	—	—	—	—	(53.2)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

Realized and unrealized investment gains and losses presented in the preceding tables represent gains and losses only for the time during which the applicable financial instruments were classified as Level 3. The transfers between levels resulted primarily from a change in observability of three inputs used to determine fair values of the securities transferred: (1) transactional data for new issuance and secondary trades, (2) broker/dealer quotes and pricing, primarily related to changes in the level of activity in the market and whether the market was considered orderly, and (3) comparable bond metrics from which to perform an analysis. For fair value measurements of financial instruments that were transferred either into or out of Level 3, we reflect the transfers using the fair value at the beginning of the period. We believe this allows for greater transparency, as all changes in fair value that arise during the reporting period of the transfer are disclosed as a component of our Level 3 reconciliation. Gains for the years ended December 31, 2014 and 2013 which are included in earnings and are attributable to the change in unrealized gains or losses relating to assets or liabilities valued using significant unobservable inputs and still held at each year end were $3.3 million and $30.7 million, respectively. These amounts relate entirely to the changes in fair value of an embedded derivative in a modified coinsurance arrangement which are reported as realized investment gains and losses.

The table below provides quantitative information regarding the significant unobservable inputs used in Level 3 fair value measurements derived from internal models. Certain securities classified as Level 3 are excluded from the table below due to limitations in our ability to obtain the underlying inputs used by external pricing sources.

	December 31, 2014		
	Fair Value (in millions of dollars)	Unobservable Input	Range/Weighted Average
Fixed Maturity Securities			
States, Municipalities, and Political Subdivisions - Private	$101.0	- Comparability Adjustment	(b) 0.25% - 1.00% / 0.71%
All Other Corporate Bonds - Private	432.8	- Comparability Adjustment	(b) 0.50% - 0.70% / 0.60%
		- Discount for Size	(c) 0.50% - 0.50% / 0.50%
		- Lack of Marketability	(d) 0.48% - 0.48% / 0.48%
		- Volatility of Credit	(e) 0.20% - 2.00% / 0.64%
		- Market Convention	(f) Priced at Par
All Other Corporate Bonds - Public	128.7	- Comparability Adjustment	(b) 0.10% - 0.50% / 0.40%
		- Lack of Marketability	(d) 0.20% - 0.35% / 0.29%
		- Volatility of Credit	(e) (0.30)% - 0.50% / (0.05)%
Equity Securities - Private	1.1	- Market Convention	(f) Priced at Cost or Owner's Equity
Embedded Derivative in Modified Coinsurance Arrangement	(49.9)	- Projected Liability Cash Flows	(g) Actuarial Assumptions

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 2 - Fair Values of Financial Instruments - Continued

	December 31, 2013		
	Fair Value (in millions of dollars)	Unobservable Input	Range/Weighted Average
Fixed Maturity Securities			
States, Municipalities, and Political Subdivisions - Private	$142.7	- Comparability Adjustment	(b) 0.25% - 1.25% / 0.65%
Mortgage/Asset-Backed Securities - Private	0.5	- Discount for Size	(c) 4.93% - 5.03% / 5.01%
All Other Corporate Bonds - Private	371.3	- Change in Benchmark Reference - Comparability Adjustment - Discount for Size - Lack of Marketability - Volatility of Credit - Market Convention	(a) 3.36% - 3.36% / 3.36% (b) (0.70)% - (0.40)% / (0.60)% (c) 0.50% - 0.50% / 0.50% (d) 0.20% - 1.00% / 0.55% (e) 0.07% - 4.00% / 0.85% (f) Priced at Par
All Other Corporate Bonds - Public	514.4	- Change in Benchmark Reference - Comparability Adjustment - Lack of Marketability - Volatility of Credit	(a) (0.32)% - 0.25% / 0.04% (b) (0.23)% - 1.00% / 0.41% (d) 0.20% - 0.20% / 0.20% (e) (0.88)% - 0.46% / (0.26)%
Equity Securities - Private	4.2	- Market Convention	(f) Priced at Cost or Owner's Equity
Embedded Derivative in Modified Coinsurance Arrangement	(53.2)	- Projected Liability Cash Flows	(g) Actuarial Assumptions

(a) Represents basis point adjustments for changes in benchmark spreads associated with various ratings categories
(b) Represents basis point adjustments for changes in benchmark spreads associated with various industry sectors
(c) Represents basis point adjustments based on issue/issuer size relative to the benchmark
(d) Represents basis point adjustments to apply a discount due to the illiquidity of an investment
(e) Represents basis point adjustments for credit-specific factors
(f) Represents a decision to price based on par value, cost, or owner's equity when limited data is available
(g) Represents various actuarial assumptions required to derive the liability cash flows including incidence, termination, and lapse rates

Isolated increases in unobservable inputs other than market convention will result in a lower fair value measurement, whereas isolated decreases will result in a higher fair value measurement. The unobservable input for market convention is not sensitive to input movements. The projected liability cash flows used in the fair value measurement of our Level 3 embedded derivative are based on expected claim payments. If claim payments increase, the projected liability cash flows will increase, resulting in a decrease in the fair value of the embedded derivative. Decreases in projected liability cash flows will result in an increase in the fair value of the embedded derivative.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments

Fixed Maturity Securities

At December 31, 2014 and 2013, all fixed maturity securities were classified as available-for-sale. In the following charts, prior year amounts have been reclassified, where applicable, between public utilities and all other corporate bonds to conform to the current year categorization of certain securities.

The amortized cost and fair values of securities by security type are shown as follows.

	December 31, 2014			
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Fair Value
	(in millions of dollars)			
United States Government and Government Agencies and Authorities	$983.5	$255.5	$0.5	$1,238.5
States, Municipalities, and Political Subdivisions	1,745.0	377.6	1.1	2,121.5
Foreign Governments	1,101.1	206.3	—	1,307.4
Public Utilities	7,046.1	1,505.4	0.9	8,550.6
Mortgage/Asset-Backed Securities	2,224.9	207.0	0.1	2,431.8
All Other Corporate Bonds	25,658.8	3,828.6	122.2	29,365.2
Redeemable Preferred Stocks	44.0	5.9	—	49.9
Total Fixed Maturity Securities	$38,803.4	$6,386.3	$124.8	$45,064.9

	December 31, 2013			
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Fair Value
	(in millions of dollars)			
United States Government and Government Agencies and Authorities	$1,028.6	$173.1	$5.6	$1,196.1
States, Municipalities, and Political Subdivisions	1,706.0	117.2	40.0	1,783.2
Foreign Governments	1,226.4	149.6	2.8	1,373.2
Public Utilities	7,121.7	901.2	25.7	7,997.2
Mortgage/Asset-Backed Securities	1,858.7	184.6	4.0	2,039.3
All Other Corporate Bonds	25,315.2	2,828.3	225.8	27,917.7
Redeemable Preferred Stocks	33.0	4.7	—	37.7
Total Fixed Maturity Securities	$38,289.6	$4,358.7	$303.9	$42,344.4

The following charts indicate the length of time our fixed maturity securities have been in a gross unrealized loss position.

	December 31, 2014			
	Less Than 12 Months		12 Months or Greater	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
	(in millions of dollars)			
	$—	$—	$7.4	$0.5

United States Government and Government Agencies and Authorities				
States, Municipalities, and Political Subdivisions	1.6	—	42.0	1.1
Public Utilities	5.1	0.2	58.2	0.7
Mortgage/Asset-Backed Securities	28.0	—	1.9	0.1
All Other Corporate Bonds	1,666.2	82.2	729.4	40.0
Total Fixed Maturity Securities	$1,700.9	$82.4	$838.9	$42.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

	December 31, 2013			
	Less Than 12 Months		12 Months or Greater	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
	(in millions of dollars)			
United States Government and Government Agencies and Authorities	$41.1	$3.1	$5.2	$2.5
States, Municipalities, and Political Subdivisions	412.5	33.5	37.2	6.5
Foreign Governments	87.2	2.8	—	—
Public Utilities	506.0	23.7	27.5	2.0
Mortgage/Asset-Backed Securities	341.0	3.6	2.5	0.4
All Other Corporate Bonds	3,776.9	197.4	238.6	28.4
Total Fixed Maturity Securities	$5,164.7	$264.1	$311.0	$39.8

The following is a distribution of the maturity dates for fixed maturity securities. The maturity dates have not been adjusted for possible calls or prepayments.

	December 31, 2014				
	Total Amortized Cost	Unrealized Gain Position		Unrealized Loss Position	
		Gross Gain	Fair Value	Gross Loss	Fair Value
	(in millions of dollars)				
1 year or less	$1,372.0	$34.3	$1,406.3	$—	$—
Over 1 year through 5 years	6,871.2	719.3	7,434.0	9.4	147.1
Over 5 years through 10 years	9,532.9	1,003.3	8,792.3	80.9	1,663.0
Over 10 years	18,802.4	4,422.4	22,490.6	34.4	699.8
	36,578.5	6,179.3	40,123.2	124.7	2,509.9
Mortgage/Asset-Backed Securities	2,224.9	207.0	2,401.9	0.1	29.9
Total Fixed Maturity Securities	$38,803.4	$6,386.3	$42,525.1	$124.8	$2,539.8

	December 31, 2013				
	Total Amortized Cost	Unrealized Gain Position		Unrealized Loss Position	
		Gross Gain	Fair Value	Gross Loss	Fair Value
	(in millions of dollars)				
1 year or less	$903.9	$20.6	$915.5	$—	$9.0
Over 1 year through 5 years	7,098.2	727.1	7,678.5	0.6	146.2
Over 5 years through 10 years	9,492.6	940.2	8,137.4	95.8	2,199.6
Over 10 years	18,936.2	2,486.2	18,441.5	203.5	2,777.4
	36,430.9	4,174.1	35,172.9	299.9	5,132.2
Mortgage/Asset-Backed Securities	1,858.7	184.6	1,695.8	4.0	343.5
Total Fixed Maturity Securities	$38,289.6	$4,358.7	$36,868.7	$303.9	$5,475.7

At December 31, 2014, the fair value of investment-grade fixed maturity securities was $41,539.7 million, with a gross unrealized gain of $6,238.0 million and a gross unrealized loss of $47.5 million. The gross unrealized loss on investment-grade fixed maturity securities was 38.1 percent of the total gross unrealized loss on fixed maturity

securities. Unrealized losses on investment-grade fixed maturity securities principally relate to changes in interest rates or changes in market or sector credit spreads which occurred subsequent to the acquisition of the securities.

At December 31, 2014, the fair value of below-investment-grade fixed maturity securities was $3,525.2 million, with a gross unrealized gain of $148.3 million and a gross unrealized loss of $77.3 million. The gross unrealized loss on below-investment-grade fixed maturity securities was 61.9 percent of the total gross unrealized loss on fixed maturity securities. Generally, below-investment-grade fixed maturity securities are more likely to develop credit concerns than investment-grade securities. At

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

December 31, 2014, the unrealized losses in our below-investment-grade fixed maturity securities were generally due to credit spreads in certain industries or sectors and, to a lesser extent, credit concerns related to specific securities. For each specific security in an unrealized loss position, we believe that there are positive factors which mitigate credit concerns and that the securities for which we have not recorded an other-than-temporary impairment will recover in value.

As of December 31, 2014, we held 75 individual investment-grade fixed maturity securities and 68 individual below-investment-grade fixed maturity securities that were in an unrealized loss position, of which 31 investment-grade fixed maturity securities and 15 below-investment-grade fixed maturity securities had been in an unrealized loss position continuously for over one year.

In determining when a decline in fair value below amortized cost of a fixed maturity security is other than temporary, we evaluate the following factors:

- Whether we expect to recover the entire amortized cost basis of the security
- Whether we intend to sell the security or will be required to sell the security before the recovery of its amortized cost basis
- Whether the security is current as to principal and interest payments
- The significance of the decline in value
- The time period during which there has been a significant decline in value
- Current and future business prospects and trends of earnings
- The valuation of the security's underlying collateral
- Relevant industry conditions and trends relative to their historical cycles
- Market conditions
- Rating agency and governmental actions
- Bid and offering prices and the level of trading activity
- Adverse changes in estimated cash flows for securitized investments
- Changes in fair value subsequent to the balance sheet date
- Any other key measures for the related security

While determining other-than-temporary impairments is a judgmental area, we utilize a formal, well-defined, and disciplined process to monitor and evaluate our fixed income investment portfolio, supported by issuer specific research and documentation as of the end of each period. The process results in a thorough evaluation of problem investments and the recording of losses on a timely basis for investments determined to have an other-than-temporary impairment.

We held no fixed maturity securities as of December 31, 2014 and 2013, for which a portion of an other-than-temporary impairment was recognized in accumulated other comprehensive income.

At December 31, 2014, we had non-binding commitments of $15.0 million to fund private placement fixed maturity securities.
Variable Interest Entities

We invest in variable interests issued by variable interest entities. These investments include tax credit partnerships, private equity partnerships, and special purpose entities. For those variable interests that are not consolidated in our financial statements, we are not the primary beneficiary because we have neither the power to direct the activities that are most significant to economic performance nor the responsibility to absorb a majority of the expected losses. The determination of whether we are the primary beneficiary is performed at the time of our initial investment and at the date of each subsequent reporting period.

As of December 31, 2014, the carrying amount of our variable interest entity investments that are not consolidated in our financial statements was $484.1 million, comprised of $289.0 million of tax credit partnerships and $195.1 million of private equity partnerships. These variable interest entity investments are reported as other long-term investments in our consolidated balance sheets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

Additionally, we recognize a liability for all legally binding unfunded commitments to these partnerships, with a corresponding recognition of an invested asset. Our liability for legally binding unfunded commitments to the tax credit partnerships was $12.8 million at December 31, 2014. Contractually, we are a limited partner in these investments, and our maximum exposure to loss is limited to the carrying value of our investment. We also had non-binding commitments of $161.6 million to fund certain private equity partnerships at December 31, 2014, the amount of which may or may not be funded.

We are the sole beneficiary of a special purpose entity which is consolidated in our financial statements. This entity is a securitized asset trust containing a highly rated bond for principal protection and a private equity partnership investment which we contributed into the trust at the time it was established. There are no restrictions on the assets held in this trust, and the trust is free to dispose of the assets at any time. The fair values of the bond and partnership were $143.9 million and $1.4 million, respectively, as of December 31, 2014 and $136.2 million and $4.4 million, respectively, as of December 31, 2013. The bond is reported as a component of fixed maturity securities, and the partnership is reported as a component of other long-term investments in our consolidated balance sheets. At December 31, 2014, we had no commitments to fund the underlying partnership, nor did we fund any amounts to the partnership during the years ended December 31, 2014, 2013, and 2012.

Mortgage Loans

Our mortgage loan portfolio is well diversified by both geographic region and property type to reduce risk of concentration. All of our mortgage loans are collateralized by commercial real estate. When issuing a new loan, our general policy is not to exceed a loan-to-value ratio, or the ratio of the loan balance to the estimated fair value of the underlying collateral, of 75 percent. We update the loan-to-value ratios at least every three years for each loan, and properties undergo a general inspection at least every two years. Our general policy for newly issued loans is to have a debt service coverage ratio greater than 1.25 times on a normalized 25 year amortization period. We update our debt service coverage ratios annually.

Mortgage loans by property type and geographic region are presented below.

	December 31					
	2014			2013		
	(in millions of dollars)					
	Carrying Amount	Percent of Total		Carrying Amount	Percent of Total	
Property Type						
Apartment	$110.1	5.9	%	$61.1	3.3	%
Industrial	542.9	29.2		567.8	31.3	
Office	794.0	42.8		776.5	42.8	
Retail	409.6	22.1		409.7	22.6	
Total	$1,856.6	100.0	%	$1,815.1	100.0	%
Region						
New England	$105.6	5.7	%	$100.9	5.6	%
Mid-Atlantic	179.4	9.7		191.5	10.5	
East North Central	210.6	11.4		244.3	13.5	
West North Central	166.2	8.9		162.3	8.9	
South Atlantic	453.6	24.4		447.7	24.7	

East South Central	75.3	4.1		67.7	3.7	
West South Central	215.6	11.6		190.9	10.5	
Mountain	116.0	6.2		101.9	5.6	
Pacific	334.3	18.0		307.9	17.0	
Total	$1,856.6	100.0	%	$1,815.1	100.0	%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

We evaluate each of our mortgage loans individually for impairment and assign an internal credit quality rating based on a comprehensive rating system used to evaluate the credit risk of the loan. The factors we use to derive our internal credit ratings may include the following:

- Loan-to-value ratio
- Debt service coverage ratio based on current operating income
- Property location, including regional economics, trends and demographics
- Age, condition, and construction quality of property
- Current and historical occupancy of property
- Lease terms relative to market
- Tenant size and financial strength
- Borrower's financial strength
- Borrower's equity in transaction
- Additional collateral, if any

Although all available and applicable factors are considered in our analysis, loan-to-value and debt service coverage ratios are the most critical factors in determining whether we will initially issue the loan and also in assigning values and determining impairment. We assign an overall rating to each loan using an internal rating scale of Aa (highest quality) to B (lowest quality). We review and adjust, as needed, our internal credit quality ratings on an annual basis. This review process is performed more frequently for mortgage loans deemed to have a higher risk of delinquency.

Mortgage loans, sorted by the applicable credit quality indicators, are as follows:

	December 31	
	2014	2013
	(in millions of dollars)	
Internal Rating		
Aa	$7.7	$10.8
A	666.0	683.1
Baa	1,156.7	1,094.6
Ba	13.1	13.5
B	13.1	13.1
Total	$1,856.6	$1,815.1
Loan-to-Value Ratio		
<= 65%	$898.7	$777.4
> 65% <= 75%	818.0	867.5
> 75% <= 85%	102.3	107.6
> 85%	37.6	62.6
Total	$1,856.6	$1,815.1

A summary of our troubled debt restructurings is as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Foreclosure			
Carrying Amount	$18.1	$4.3	$17.3

Number of Loans	1	1	3

We had no realized losses on loan foreclosures for the years ended December 31, 2014, 2013, and 2012 other than the initial impairment losses recognized prior to foreclosure. During 2014, we modified the terms of a mortgage loan with a carrying value of $18.1 million, recognized a $3.0 million realized loss on the troubled debt restructuring, and foreclosed on the property in a subsequent quarter of 2014.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

At December 31, 2014 and 2013, we held no mortgage loans that were on nonaccrual status or past due regarding principal and/or interest payments.

There have been no changes to our accounting policies or methodology from the prior period regarding estimating the allowance for credit losses on our mortgage loans. The activity in the allowance for credit losses is as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Balance at Beginning of Year	$1.5	$1.5	$1.5
Provision	3.0	—	1.8
Charge-offs, Net of Recoveries	(3.0)	—	(1.8)
Balance at End of Year	$1.5	$1.5	$1.5

As of December 31, 2014 and 2013 we held one impaired mortgage loan with an unpaid principal balance of $14.6 million, a related allowance for credit losses of $1.5 million, and a carrying value of $13.1 million.

Our average investment in impaired mortgage loans was $26.7 million, $14.9 million, and $19.1 million for the years ended December 31, 2014, 2013, and 2012, respectively. For the years ended December 31, 2014, 2013, and 2012, we recognized $1.0 million, $0.8 million, and $0.8 million, respectively, of interest income on mortgage loans subsequent to impairment.

At December 31, 2014, we had non-binding commitments of $49.3 million to fund certain commercial mortgage loans, the amount of which may or may not be funded.

Transfers of Financial Assets

To manage our cash position more efficiently, we may enter into repurchase agreements with unaffiliated financial institutions. We generally use repurchase agreements as a means to finance the purchase of invested assets or for short-term general business purposes until projected cash flows become available from our operations or existing investments. Our repurchase agreements are typically outstanding for less than 30 days. We post collateral through our repurchase agreement transactions whereby the counterparty commits to purchase securities with the agreement to resell them to us at a later, specified date. The fair value of collateral posted is generally 102 percent of the cash received.

Our investment policy also permits us to lend fixed maturity securities to unaffiliated financial institutions in short-term securities lending agreements. These agreements increase our investment income with minimal risk. Our securities lending policy requires that a minimum of 102 percent of the fair value of the securities loaned be maintained as collateral. Generally, cash is received as collateral under these agreements and is typically reinvested in short-term investments. In the event that securities are received as collateral, we are not permitted to sell or re-post them.

As of December 31, 2014, the carrying amount of fixed maturity securities loaned to third parties under our securities lending program was $176.5 million, for which we received collateral in the form of cash and securities of $58.4 million and $128.5 million, respectively. As of December 31, 2013, the carrying amount of fixed maturity securities loaned to third parties under our securities lending program was $201.6 million, for which we received collateral in

the form of cash and securities of $76.5 million and $132.9 million, respectively. We had no outstanding repurchase agreements at December 31, 2014 or 2013.

During 2014, we were approved for membership of the Federal Home Loan Bank System (FHLB). As a member, we obtain access to low-cost funding and also receive dividends based on our stock ownership. Membership requires that we purchase a minimum amount of FHLB common stock based on a percentage of our total assets. Additional common stock purchases are required based upon the amount of funds borrowed from the FHLB. We will be required to post mortgage-related assets, U.S. Treasury securities, or other acceptable forms of collateral for any borrowings we make from the FHLB. As of December 31, 2014 we had not funded any FHLB common stock purchases or obtained any advances from the FHLB. We expect to fund our initial common stock membership purchase in the first quarter of 2015 at a cost of approximately $17.7 million, $12.5 million of which was a non-binding commitment as of December 31, 2014.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

Offsetting of Financial Instruments

We enter into master netting agreements with each of our derivatives counterparties. These agreements provide for conditional rights of set-off upon the occurrence of an early termination event. An early termination event is considered a default, and it allows the non-defaulting party to offset its contracts in a loss position against any gain positions or payments due to the defaulting party. Under our agreements, default type events are defined as failure to pay or deliver as contractually agreed, misrepresentation, bankruptcy, or merger without assumption. See Note 4 for further discussion of collateral related to our derivative contracts.

We have securities lending agreements with unaffiliated financial institutions that post collateral to us in return for the use of our fixed maturity securities. A right of set-off exists that allows us to keep and apply collateral received in the event of default by the counterparty. Default within a securities lending agreement would typically occur if the counterparty failed to return the securities borrowed from us as contractually agreed. In addition, if we default by not returning collateral received, the counterparty has a right of set-off against our securities or any other amounts due to us.

Shown below are our financial instruments that either meet the accounting requirements that allow them to be offset in our balance sheets or that are subject to an enforceable master netting arrangement or similar agreement. Our accounting policy is to not offset these financial instruments in our balance sheets. Net amounts disclosed below have been reduced by the amount of collateral pledged to or received from our counterparties.

	December 31, 2014					
	Gross Amount of Recognized Financial Instruments	Gross Amount Offset in Balance Sheet	Net Amount Presented in Balance Sheet	Gross Amount Not Offset in Balance Sheet		
				Financial Instruments	Cash Collateral	Net Amount
	(in millions of dollars)					
Financial Assets:						
Derivatives	$28.0	$—	$28.0	$(7.2)	$(15.4)	$5.4
Securities Lending	176.5	—	176.5	(118.1)	(58.4)	—
Total	$204.5	$—	$204.5	$(125.3)	$(73.8)	$5.4
Financial Liabilities:						
Derivatives	$92.9	$—	$92.9	$(67.0)	$—	$25.9
Securities Lending	58.4	—	58.4	(58.4)	—	—
Total	$151.3	$—	$151.3	$(125.4)	$—	$25.9

	December 31, 2013					
	Gross Amount of Recognized Financial Instruments	Gross Amount Offset in Balance Sheet	Net Amount Presented in Balance Sheet	Gross Amount Not Offset in Balance Sheet		
				Financial Instruments	Cash Collateral	Net Amount
	(in millions of dollars)					
Financial Assets:						
Derivatives	$10.8	$—	$10.8	$(9.5)	$(1.1)	$0.2
Securities Lending	201.6	—	201.6	(125.1)	(76.5)	—

Total	$212.4	$—	$212.4	$(134.6)	$(77.6)	$0.2
Financial Liabilities:						
Derivatives	$135.6	$—	$135.6	$(98.6)	$—	$37.0
Securities Lending	76.5	—	76.5	(76.5)	—	—
Total	$212.1	$—	$212.1	$(175.1)	$—	$37.0

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 3 - Investments - Continued

Net Investment Income

Net investment income reported in our consolidated statements of income is as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Fixed Maturity Securities	$2,344.4	$2,371.6	$2,404.0
Derivatives	40.4	35.2	28.9
Mortgage Loans	109.8	109.2	107.1
Policy Loans	16.3	15.7	14.8
Other Long-term Investments	23.0	18.0	15.2
Short-term Investments	2.4	2.4	4.3
Gross Investment Income	2,536.3	2,552.1	2,574.3
Less Investment Expenses	29.0	29.5	26.9
Less Investment Income on Participation Fund Account Assets	15.1	15.7	16.1
Less Amortization of Tax Credit Partnerships	14.8	14.8	16.1
Net Investment Income	$2,477.4	$2,492.1	$2,515.2

Realized Investment Gain and Loss

Realized investment gains and losses are as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Fixed Maturity Securities			
Gross Gains on Sales	$9.3	$15.8	$29.3
Gross Losses on Sales	(7.5)	(45.7)	(20.4)
Other-Than-Temporary Impairment Loss	(13.5)	(0.8)	—
Mortgage Loans and Other Invested Assets			
Gross Gains on Sales	21.2	15.6	5.0
Gross Losses on Sales	(0.8)	—	(4.3)
Impairment Loss	(3.4)	(2.0)	(1.9)
Embedded Derivative in Modified Coinsurance Arrangement	3.3	30.7	51.8
All Other Derivatives	11.0	(1.9)	—
Foreign Currency Transactions	(3.5)	(4.9)	(3.3)
Net Realized Investment Gain	$16.1	$6.8	$56.2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 4 - Derivative Financial Instruments

Purpose of Derivatives

We are exposed to certain risks relating to our ongoing business operations. The primary risks managed by using derivative instruments are interest rate risk, risk related to matching duration for our assets and liabilities, foreign currency risk, and credit risk. Historically, we have utilized current and forward interest rate swaps and options on forward interest rate swaps and U.S. Treasury rates, current and forward currency swaps, forward treasury locks, currency forward contracts, forward contracts on specific fixed income securities, and credit default swaps. Transactions hedging interest rate risk are primarily associated with our individual and group long-term care and individual and group disability products. All other product portfolios are periodically reviewed to determine if hedging strategies would be appropriate for risk management purposes. We do not use derivative financial instruments for speculative purposes.

Derivatives designated as cash flow hedges and used to reduce our exposure to interest rate and duration risk are as follows:

- Interest rate swaps are used to hedge interest rate risks and to improve the matching of assets and liabilities. An interest rate swap is an agreement in which we agree with other parties to exchange, at specified intervals, the difference between fixed rate and variable rate interest amounts. We use interest rate swaps to hedge the anticipated purchase of fixed maturity securities thereby protecting us from the potential adverse impact of declining interest rates on the associated policy reserves. We also use interest rate swaps to hedge the potential adverse impact of rising interest rates in anticipation of issuing fixed rate long-term debt.

- Forward treasury locks are used to minimize interest rate risk associated with the anticipated purchase or disposal of fixed maturity securities. A forward treasury lock is a derivative contract without an initial investment where we and the counterparty agree to purchase or sell a specific U.S. Treasury bond at a future date at a pre-determined price.

- Options on U.S. Treasury rates are used to hedge the interest rate risk associated with the anticipated purchase of fixed maturity securities. These options give us the right, but not the obligation, to receive a specific interest rate for a specified period of time. These options enable us to lock in a minimum investment yield to hedge the potential adverse impact of declining interest rates.

Derivatives designated as fair value hedges and used to reduce our exposure to interest rate and duration risk are as follows:

- Interest rate swaps are used to effectively convert certain of our fixed rate securities into floating rate securities which are used to fund our floating rate long-term debt. Under these swap agreements, we receive a variable rate of interest and pay a fixed rate of interest. Additionally, we use interest rate swaps to effectively convert certain fixed rate, long-term debt into floating rate long-term debt. Under these swap agreements, we receive a fixed rate of interest and pay a variable rate of interest.

Derivatives designated as cash flow hedges and used to reduce our exposure to foreign currency risk are as follows:

- Foreign currency interest rate swaps have historically been used to hedge the currency risk of certain foreign currency-denominated fixed maturity securities owned for portfolio diversification and to hedge the currency risk associated with certain of the principal and interest payments of the U.S. dollar-denominated debt issued by one of our

U.K. subsidiaries. For hedges of fixed maturity securities, we agree to pay, at specified intervals, fixed rate foreign currency-denominated principal and interest payments in exchange for fixed rate payments in the functional currency of the operating segment. For hedges of debt issued, we agree to pay, at specified intervals, fixed rate foreign currency-denominated principal and interest payments to the counterparty in exchange for fixed rate U.S. dollar-denominated principal and interest payments.

Derivatives not designated as hedging instruments and used to reduce our exposure to foreign currency risk and credit losses on securities owned are as follows:

- Foreign currency interest rate swaps previously designated as hedges were used to hedge the currency risk of certain foreign currency-denominated fixed maturity securities owned for portfolio diversification. We agree to pay, at specified intervals, fixed rate foreign currency-denominated principal and interest payments in exchange for fixed rate

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 4 - Derivative Financial Instruments - Continued

payments in the functional currency of the operating segment. We hold offsetting swaps wherein we agree to pay fixed rate principal and interest payments in the functional currency of the operating segment in exchange for fixed rate foreign currency-denominated payments.

- Credit default swaps are used as economic hedges against credit risk but do not qualify for hedge accounting. A credit default swap is an agreement in which we agree with another party to pay, at specified intervals, a fixed-rate fee in exchange for insurance against a credit event on a specific investment. If a defined credit event occurs, our counterparty may either pay us a net cash settlement, or we may surrender the specific investment to them in exchange for cash equal to the full notional amount of the swap. Credit events typically include events such as bankruptcy, failure to pay, or certain types of debt restructuring.

Derivative Risks

The basic types of risks associated with derivatives are market risk (that the value of the derivative will be adversely impacted by changes in the market, primarily the change in interest and exchange rates) and credit risk (that the counterparty will not perform according to the terms of the contract). The market risk of the derivatives should generally offset the market risk associated with the hedged financial instrument or liability. To help limit the credit exposure of the derivatives, we enter into master netting agreements with our counterparties whereby contracts in a gain position can be offset against contracts in a loss position. We also typically enter into bilateral, cross-collateralization agreements with our counterparties to help limit the credit exposure of the derivatives. These agreements require the counterparty in a loss position to submit acceptable collateral with the other counterparty in the event the net loss position meets or exceeds an agreed upon amount. Our current credit exposure on derivatives, which is limited to the value of those contracts in a net gain position, including accrued interest receivable less collateral held, was $13.6 million at December 31, 2014. We held cash collateral from our counterparties of $15.4 million and $1.1 million at December 31, 2014 and 2013, respectively. We post either fixed maturity securities or cash as collateral to our counterparties. The carrying value of fixed maturity securities posted as collateral to our counterparties was $67.0 million and $95.6 million at December 31, 2014 and 2013, respectively. We had no cash posted as collateral to our counterparties at December 31, 2014 and 2013. See Note 3 for further discussion of our master netting agreements.

The majority of our derivative instruments contain provisions that require us to maintain specified issuer credit ratings and financial strength ratings. Should our ratings fall below these specified levels, we would be in violation of the provisions, and our derivatives counterparties could terminate our contracts and request immediate payment. The aggregate fair value of all derivative instruments with credit risk-related contingent features that were in a liability position was $92.9 million and $135.6 million at December 31, 2014 and 2013, respectively.

Derivative Transactions

The table below summarizes, by notional amounts, the activity for each category of derivatives. The notional amounts represent the basis upon which our counterparty pay and receive amounts are calculated.

	Swaps						
	Receive Variable/Pay Fixed	Receive Fixed/Pay Fixed	Receive Fixed/Pay Variable	Credit Default	Forwards	Options	Total
(in millions of dollars)							

Balance at December 31, 2011	$174.0	$554.0	$685.0	$—	$—	$—	$1,413.0
Additions	—	—	250.0	—	86.0	—	336.0
Terminations	—	45.2	185.0	—	86.0	—	316.2
Balance at December 31, 2012	174.0	508.8	750.0	—	—	—	1,432.8
Additions	—	160.0	—	97.0	24.0	10.0	291.0
Terminations	24.0	38.4	150.0	—	24.0	10.0	246.4
Balance at December 31, 2013	150.0	630.4	600.0	97.0	—	—	1,477.4
Additions	—	250.1	—	—	68.0	—	318.1
Terminations	—	40.1	—	—	68.0	—	108.1
Balance at December 31, 2014	$150.0	$840.4	$600.0	$97.0	$—	$—	$1,687.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 4 - Derivative Financial Instruments - Continued

Cash Flow Hedges

As of December 31, 2014 and 2013, we had $618.0 million and $630.4 million, respectively, notional amount of receive fixed, pay fixed, open current and forward foreign currency interest rate swaps to hedge fixed income foreign currency-denominated securities and U.S. dollar-denominated debt issued by one of our U.K. subsidiaries.

During 2014, we novated certain of our foreign currency interest rate swaps with a notional amount of $97.0 million and a fair value of $(29.5) million to a new counterparty. At the time of novation, these derivatives were effective hedges, and we therefore deferred the unrealized loss into other comprehensive income and will recognize the loss in earnings during the periods in which the hedged items affect earnings. In conjunction with the novation, these derivatives were de-designated as hedges, and subsequent changes in their fair value will be reported in earnings as a component of net realized investment gain or loss. To establish a new effective hedging relationship with the fixed income foreign currency denominated securities previously hedged, we entered into $124.7 million notional amount of foreign currency interest rate swaps during 2014 whereby we receive fixed rate functional currency principal and interest in exchange for fixed rate payments in foreign currency.

During 2014, we redeemed a portion of the outstanding principal of the U.S. dollar-denominated debt issued by one of our U.K. subsidiaries. In conjunction with this redemption, we reclassified $13.1 million of the deferred gain on cash flow hedges from accumulated other comprehensive income to realized investment gain in our consolidated statements of income. This amount represents the applicable portion of the deferred gain from previously terminated derivatives associated with the hedge of this debt. See Note 8.

During 2013, we entered into $150.0 million notional amount of foreign currency swaps to hedge the currency risk on a portion of the U.S. dollar-denominated debt issued by one of our U.K. subsidiaries. Also during 2013, we terminated, as scheduled, $150.0 million notional amount of received fixed, pay variable forward starting interest rate swaps used to hedge the anticipated purchase of fixed maturity securities.

For the years ended December 31, 2014, 2013, and 2012 there was no material ineffectiveness related to our cash flow hedges, and no component of the derivative instruments' gain or loss was excluded from the assessment of hedge effectiveness.

As of December 31, 2014, we expect to amortize approximately $50.2 million of net deferred gains on derivative instruments during the next twelve months. This amount will be reclassified from accumulated other comprehensive income into earnings and reported on the same income statement line item as the hedged item. The income statement line items that will be affected by this amortization are net investment income and interest and debt expense. The remaining principal balance of the U.S. dollar-denominated debt issued by one of our U.K. subsidiaries is scheduled to mature during the fourth quarter of 2015, at which time we will reclassify the remaining deferred cash flow hedge gain of approximately $28.4 million from accumulated other comprehensive income to realized investment gain in our consolidated statements of income. Additional amounts that may be reclassified from accumulated other comprehensive income into earnings to offset the earnings impact of foreign currency translation of hedged items are not estimable.

As of December 31, 2014, we are hedging the variability of future cash flows associated with forecasted transactions through the year 2038.

Fair Value Hedges

As of December 31, 2014 and 2013, we had $150.0 million notional amount of receive variable, pay fixed interest rate swaps to hedge the changes in fair value of certain fixed rate securities held. These swaps effectively convert the associated fixed rate securities into floating rate securities, which are used to fund our floating rate long-term debt. The change in fair value of the hedged fixed maturity securities attributable to the hedged benchmark interest rate resulted in a loss of $5.3 million, $11.5 million, and $1.2 million for the years ended December 31, 2014, 2013, and 2012, respectively, with an offsetting gain on the related interest rate swaps.

As of December 31, 2014 and 2013, we had $600.0 million notional amount of receive fixed, pay variable interest rate swaps to hedge the changes in the fair value of certain fixed rate long-term debt. These swaps effectively convert the associated fixed rate long-term debt into floating rate debt and provide for a better matching of interest rates with our short-term investments, which

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 4 - Derivative Financial Instruments - Continued

have frequent interest rate resets similar to a floating rate security. The change in fair value of the hedged debt attributable to the hedged benchmark interest rate resulted in a gain (loss) of $(5.5) million, $21.1 million, and $(6.6) million for the years ended December 31, 2014, 2013, and 2012, respectively, with an offsetting gain or loss on the related interest rate swaps.

For the years ended December 31, 2014, 2013, and 2012, there was no material ineffectiveness related to our fair value hedges, and no component of the derivative instruments' gain or loss was excluded from the assessment of hedge effectiveness. There were no instances wherein we discontinued fair value hedge accounting due to a hedged firm commitment no longer qualifying as a fair value hedge.

Derivatives not Designated as Hedging Instruments

During 2014, we entered into $125.4 million notional amount of foreign currency interest rate swaps in conjunction with the previously discussed transaction wherein we de-designated foreign currency interest rate swaps with a notional amount of $97.0 million. The derivatives were not designated as hedges, and as such, changes in fair value related to these derivatives will be reported in earnings as a component of net realized investment gain or loss. We expect the changes in fair value of these derivatives to materially offset the changes in fair value related to the de-designated derivatives.

As of December 31, 2014 and 2013, we held $97.0 million notional amount of single name credit default swaps. We entered into these swaps in order to mitigate the credit risk associated with specific securities owned.

We have an embedded derivative in a modified coinsurance arrangement for which we include in our realized investment gains and losses a calculation intended to estimate the value of the option of our reinsurance counterparty to cancel the reinsurance contract with us. However, neither party can unilaterally terminate the reinsurance agreement except in extreme circumstances resulting from regulatory supervision, delinquency proceedings, or other direct regulatory action. Cash settlements or collateral related to this embedded derivative are not required at any time during the reinsurance contract or at termination of the reinsurance contract. There are no credit-related counterparty triggers, and any accumulated embedded derivative gain or loss reduces to zero over time as the reinsured business winds down.

Locations and Amounts of Derivative Financial Instruments

The following tables summarize the location and fair values of derivative financial instruments, as reported in our consolidated balance sheets.

	December 31, 2014			
	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
	(in millions of dollars)			
Designated as Hedging Instruments				
Interest Rate Swaps	Other L-T Investments	$5.7	Other Liabilities	$20.8
Foreign Exchange Contracts	Other L-T Investments	22.3	Other Liabilities	39.6
Total		$28.0		$60.4

Not Designated as Hedging Instruments		
Credit Default Swaps	Other Liabilities	$1.2
Foreign Exchange Contracts	Other Liabilities	31.3
Embedded Derivative in Modified Coinsurance Arrangement	Other Liabilities	49.9
Total		$82.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 4 - Derivative Financial Instruments - Continued

	December 31, 2013			
	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
	(in millions of dollars)			
Designated as Hedging Instruments				
Interest Rate Swaps	Other L-T Investments	$9.2	Other Liabilities	$35.0
Foreign Exchange Contracts	Other L-T Investments	1.6	Other Liabilities	98.7
Total		$10.8		$133.7
Not Designated as Hedging Instruments				
Credit Default Swaps			Other Liabilities	$1.9
Embedded Derivative in Modified Coinsurance Arrangement			Other Liabilities	53.2
Total				$55.1

The following table summarizes the location of gains and losses on the effective portion of derivative financial instruments designated as cash flow hedging instruments, as reported in our consolidated statements of income and consolidated statements of comprehensive income.

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Gain (Loss) Recognized in Other Comprehensive Income (Loss) on Derivatives			
Interest Rate Swaps and Forwards	$(0.1)	$(7.2)	$77.9
Options	—	(0.1)	—
Foreign Exchange Contracts	16.2	22.6	3.5
Total	$16.1	$15.3	$81.4
Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Income			
Net Investment Income			
Interest Rate Swaps and Forwards	$47.8	$43.1	$40.0
Foreign Exchange Contracts	(4.2)	(5.9)	(5.3)
Net Realized Investment Gain (Loss)			
Interest Rate Swaps	4.3	1.3	4.1
Foreign Exchange Contracts	6.9	(13.8)	(17.0)
Interest and Debt Expense			
Interest Rate Swaps	(1.8)	(1.7)	(1.7)
Total	$53.0	$23.0	$20.1

The following table summarizes the location of gains and losses on our derivatives not designated as hedging instruments, as reported in our consolidated statements of income.

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		

Net Realized Investment Gain (Loss)			
Credit Default Swaps	$(0.3)	$(1.9)	$—
Foreign Exchange Contracts	(1.8)	—	—
Embedded Derivative in Modified Coinsurance Arrangement	3.3	30.7	51.8
Total	$1.2	$28.8	$51.8

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 5 - Accumulated Other Comprehensive Income

Components of our accumulated other comprehensive income, after tax, and related changes are as follows:

	Net Unrealized Gain on Securities	Net Gain on Cash Flow Hedges	Foreign Currency Translation Adjustment	Unrecognized Pension and Postretirement Benefit Costs	Total
	(in millions of dollars)				
Balance at December 31, 2012	$873.5	$401.6	$(72.6)	$(574.5)	$628.0
Other Comprehensive Income (Loss) Before Reclassifications	(746.4)	9.7	25.5	328.6	(382.6)
Amounts Reclassified from Accumulated Other Comprehensive Income or Loss	8.6	(15.0)	—	16.0	9.6
Net Other Comprehensive Income (Loss)	(737.8)	(5.3)	25.5	344.6	(373.0)
Balance at December 31, 2013	135.7	396.3	(47.1)	(229.9)	255.0
Other Comprehensive Income (Loss) Before Reclassifications	154.3	31.1	(66.3)	(216.1)	(97.0)
Amounts Reclassified from Accumulated Other Comprehensive Income or Loss	0.3	(36.4)	—	44.5	8.4
Net Other Comprehensive Income (Loss)	154.6	(5.3)	(66.3)	(171.6)	(88.6)
Balance at December 31, 2014	$290.3	$391.0	$(113.4)	$(401.5)	$166.4

The net unrealized gain on securities consists of the following components:

	December 31			Change for the Year Ended December 31	
	2014	2013	2012	2014	2013
	(in millions of dollars)				
Fixed Maturity Securities	$6,261.5	$4,054.8	$7,221.5	$2,206.7	$(3,166.7)
Other Investments	13.9	55.5	92.8	(41.6)	(37.3)
Deferred Acquisition Costs	(50.8)	(41.6)	(67.0)	(9.2)	25.4
Reserves for Future Policy and Contract Benefits	(6,150.3)	(4,108.5)	(6,277.5)	(2,041.8)	2,169.0
Reinsurance Recoverable	365.0	263.8	351.5	101.2	(87.7)
Income Tax	(149.0)	(88.3)	(447.8)	(60.7)	359.5
Total	$290.3	$135.7	$873.5	$154.6	$(737.8)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 5 - Accumulated Other Comprehensive Income - Continued

Amounts reclassified from accumulated other comprehensive income were recognized in our consolidated statements of income as follows:

	Year Ended December 31	
	2014	2013
	(in millions of dollars)	
Net Unrealized Gain on Securities		
Net Realized Investment Gain (Loss)		
Gain (Loss) on Sales of Securities and Other Invested Assets	$12.6	$(12.6)
Other-Than-Temporary Impairment Loss	(13.5)	(0.8)
	(0.9)	(13.4)
Income Tax Benefit	(0.6)	(4.8)
Total	$(0.3)	$(8.6)
Net Gain on Cash Flow Hedges		
Net Investment Income		
Gain on Interest Rate Swaps and Forwards	$47.8	$43.1
Loss on Foreign Exchange Contracts	(4.2)	(5.9)
Net Realized Investment Gain (Loss)		
Gain on Interest Rate Swaps	4.3	1.3
Gain (Loss) on Foreign Exchange Contracts	6.9	(13.8)
Interest and Debt Expense		
Loss on Interest Rate Swaps	(1.8)	(1.7)
	53.0	23.0
Income Tax Expense	16.6	8.0
Total	$36.4	$15.0
Unrecognized Pension and Postretirement Benefit Costs		
Other Expenses		
Amortization of Net Actuarial Loss	$(5.6)	$(32.9)
Amortization of Prior Service Credit	1.7	5.0
Curtailment Gain	—	3.0
Settlement Loss	(64.4)	—
	(68.3)	(24.9)
Income Tax Benefit	(23.8)	(8.9)
Total	$(44.5)	$(16.0)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 6 - Liability for Unpaid Claims and Claim Adjustment Expenses

Changes in the liability for unpaid claims and claim adjustment expenses are as follows:

	2014	2013	2012
	(in millions of dollars)		
Balance at January 1	$24,535.6	$24,567.1	$24,586.5
Less Reinsurance Recoverable	2,072.8	2,006.0	2,042.6
Net Balance at January 1	22,462.8	22,561.1	22,543.9
Incurred Related to			
Current Year	4,851.5	4,751.9	4,946.2
Prior Years			
Interest	1,214.7	1,230.0	1,247.6
All Other Incurred	(13.5)	(44.7)	(175.7)
Foreign Currency	(138.7)	41.2	101.1
Total Incurred	5,914.0	5,978.4	6,119.2
Paid Related to			
Current Year	(1,702.3)	(1,657.3)	(1,715.4)
Prior Years	(4,547.4)	(4,419.4)	(4,386.6)
Total Paid	(6,249.7)	(6,076.7)	(6,102.0)
Net Balance at December 31	22,127.1	22,462.8	22,561.1
Plus Reinsurance Recoverable	2,066.9	2,072.8	2,006.0
Balance at December 31	$24,194.0	$24,535.6	$24,567.1

The majority of the net balances are related to disability claims with long-tail payouts on which interest earned on assets backing liabilities is an integral part of pricing and reserving. Interest accrued on prior year reserves has been calculated on the opening reserve balance less one-half year's cash payments at our average reserve discount rate used during 2014, 2013, and 2012.

"Incurred Related to Prior Years - All Other Incurred" for the years shown in the preceding chart includes the reserve adjustments as discussed in the following paragraphs, which create variances year over year. Excluding those adjustments, the variability exhibited year over year is caused primarily by the level of claim resolutions in the period relative to the long-term expectations reflected in the reserves. Our claim resolution rate assumption used in determining reserves is our expectation of the resolution rate we will experience over the life of the block of business and will vary from actual experience in any one period, both favorably and unfavorably.

2014 Long-term Care Reserve Increase

Policy reserves for our long-term care block of business are determined using the gross premium valuation method and, prior to the fourth quarter of 2014, were valued based on assumptions established as of December 31, 2011, the date of the initial loss recognition. Gross premium valuation assumptions do not change after the date of loss recognition unless reserves are again determined to be deficient. We undertake a review of policy reserve adequacy annually during the fourth quarter of each year, or more frequently if appropriate, using best estimate assumptions as of the date of the review.

Included in our fourth quarter of 2014 review was an analysis of our reserve assumptions, including those for the discount rate, mortality and morbidity rates, persistency, and premium rate increases. Our analysis of reserve discount rate assumptions considered the continued historic low interest rate environment, future market expectations, and our view of future portfolio yields. The assumptions we established in 2011 were set at a level that we estimated would be sustainable in a low interest rate environment for three to five years, with improvements in market yields beginning after the third year. Since that time, however, interest rates have continued to hover near historic lows, and credit spreads have tightened. Our assumption update for mortality incorporates the last three years of Company-specific experience and emerging trends as well as industry data, where available and appropriate, and reflects improvements in life expectancies beyond what was initially anticipated in 2011. Our morbidity assumptions were updated to reflect trends from our own emerging Company experience in claim incidence and terminations, as

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 6 - Liability for Unpaid Claims and Claim Adjustment Expenses - Continued

well as trends based on available and appropriate industry data and studies. Our premium rate increase assumptions were updated to reflect progress-to-date and our on-going rate increase strategy.

Based on our analysis, as of December 31, 2014 we lowered the discount rate assumption to reflect the low interest rate environment and our revised expectation of future investment portfolio yield rates. Our revised assumptions anticipate the low interest rate environment persisting for the next three to five years, with a return to more historical averages over the following five year period. We updated our mortality assumptions to reflect emerging experience due to an increase in life expectancies which increases the ultimate number of people who will utilize long-term care benefits and also lengthens the amount of time a claimant may receive long-term care benefits. We changed our morbidity assumptions to reflect emerging industry experience as well as our own Company experience, and we updated our projection of future premium rate increase approvals. Using our revised best estimate assumptions, as of December 31, 2014 we determined that our policy and claim reserves should be increased $698.2 million to reflect our current estimate of future benefit obligations. Of this amount, $85.8 million was related to claim reserves, which can be attributed to prior year incurred claims, thereby impacting the results shown in the preceding chart.

2013 Unclaimed Death Benefits Reserve Increase

Beginning in 2011, a number of state regulators began requiring insurers to cross-check specified insurance policies with the Social Security Administration’s Death Master File to identify potential matches. If a potential match was identified, insurers were requested to determine if benefits were due, locate beneficiaries, and make payments where appropriate. We initiated this process where requested, and in 2012 we began implementing this process in all states on a forward-looking basis. In addition to implementing this on a forward-looking basis, in 2013 we began an initiative to search for potential claims from previous years.
During 2013, we completed our assessment of benefits which we estimate will be paid under this initiative, and as such, established $95.5 million of additional claim reserves for payment of these benefits. Claim reserves were increased $49.1 million for Unum US group life, $26.3 million for Unum US voluntary life, and $20.1 million for Colonial Life voluntary life. The reserves established were attributed to prior year incurred claims, thereby impacting the results shown in the preceding chart.

2013 Group Life Waiver of Premium Benefit Reserve Reduction

Within our Unum US segment, we offer group life insurance coverage which consists primarily of renewable term life insurance and includes a provision for waiver of premium, if disabled. The group life waiver of premium benefit (group life waiver) provides for continuation of life insurance coverage when an insured, or the employer on behalf of the insured, is no longer paying premium because the employee is not actively at work due to a disability. The group life waiver claim reserve is the present value of future anticipated death benefits reflecting the probability of death while remaining disabled. Claim reserves are calculated using assumptions based on past experience adjusted for current trends and any other factors that would modify past experience and are subject to revision as current claim experience emerges and alters our view of future expectations. The two fundamental assumptions in the development of the group life waiver reserve are mortality and recovery. Our emerging experience and that which continues to emerge within the industry indicate an increase in life expectancies, which decreases the ultimate anticipated death benefits to be paid under the group life waiver benefit. Emerging experience also reflects an improvement in claim recovery rates, which also lessens the likelihood of payment of a death benefit while the insured is disabled. During 2013, we completed a review of our assumptions and modified our mortality and claim recovery assumptions for our Unum US group life waiver reserves and, as a result, reduced claim reserves by $85.0 million. Of this amount,

approximately $78.0 million was attributed to prior year incurred claims, thereby impacting the results shown in the preceding chart.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 6 - Liability for Unpaid Claims and Claim Adjustment Expenses - Continued

Reconciliation

A reconciliation of policy and contract benefits and reserves for future policy and contract benefits as reported in our consolidated balance sheets to the liability for unpaid claims and claim adjustment expenses is as follows:

	December 31		
	2014	2013	2012
	(in millions of dollars)		
Policy and Contract Benefits	$1,529.3	$1,511.0	$1,484.6
Reserves for Future Policy and Contract Benefits	45,929.4	43,099.1	44,694.4
Total	47,458.7	44,610.1	46,179.0
Less:			
Life Reserves for Future Policy and Contract Benefits	7,850.9	7,740.5	7,571.1
Accident and Health Active Life Reserves	9,263.5	8,225.5	7,763.3
Unrealized Adjustment to Reserves for Future Policy and Contract Benefits	6,150.3	4,108.5	6,277.5
Liability for Unpaid Claims and Claim Adjustment Expenses	$24,194.0	$24,535.6	$24,567.1

The unrealized adjustment to reserves for future policy and contract benefits reflects the changes that would be necessary to policyholder liabilities if the unrealized investment gains and losses related to the corresponding available-for-sale securities had been realized. Changes in this adjustment are reported as a component of other comprehensive income or loss.

Note 7 - Income Tax

Total income tax expense (benefit) is allocated as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Net Income	$113.8	$347.1	$355.1
Stockholders' Equity - Additional Paid-in Capital			
Stock-Based Compensation	(3.0)	(0.8)	3.5
Stockholders' Equity - Accumulated Other Comprehensive Income (Loss)			
Change in Net Unrealized Gain on Securities Before Adjustment	725.8	(1,102.8)	467.7
Change in Adjustment to Deferred Acquisition Costs and Reserves for Future Policy and Contract Benefits, Net of Reinsurance	(665.1)	743.3	(325.6)
Change in Net Gain on Cash Flow Hedges	(2.0)	(1.3)	(4.3)
Change in Unrecognized Pension and Postretirement Benefit Costs	(92.4)	185.2	(68.0)
Total	$77.1	$170.7	$428.4

A reconciliation of the income tax expense (benefit) attributable to income from operations before income tax, computed at U.S. federal statutory tax rates, to the income tax expense (benefit) as included in our consolidated statements of income, is as follows. Certain prior year amounts have been reclassified to conform to current year reporting.

Year Ended December 31

	2014		2013		2012	
Statutory Income Tax	35.0	%	35.0	%	35.0	%
Foreign Items	(4.3	)	(1.8	)	(1.9	)
Tax Credits	(8.1	)	(3.4	)	(2.7	)
Tax-exempt Investment Income	(2.3	)	(1.0	)	(0.9	)
Other Items, Net	1.3		—		(1.1	)
Effective Tax	21.6	%	28.8	%	28.4	%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 7 - Income Tax - Continued

Our net deferred tax liability consists of the following:

	December 31	
	2014	2013
	(in millions of dollars)	
Deferred Tax Liability		
Deferred Acquisition Costs	$97.4	$70.0
Fixed Assets	93.0	80.3
Invested Assets	1,999.2	1,274.3
Other	64.6	54.4
Gross Deferred Tax Liability	2,254.2	1,479.0
Deferred Tax Asset		
Reserves	1,919.2	1,180.1
Employee Benefits	254.0	151.2
Other	2.6	3.4
Gross Deferred Tax Asset	2,175.8	1,334.7
Total Net Deferred Tax Liability	$78.4	$144.3

Our consolidated statements of income include amounts subject to both domestic and foreign taxation. The income and related tax expense (benefit) are as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Income Before Tax			
United States - Federal	$376.9	$1,072.0	$1,128.4
Foreign	150.3	133.2	121.1
Total	$527.2	$1,205.2	$1,249.5
Current Tax Expense (Benefit)			
United States - Federal	$128.4	$277.9	$164.4
Foreign	(25.1)	18.7	42.2
Total	103.3	296.6	206.6
Deferred Tax Expense (Benefit)			
United States - Federal	(44.4)	47.3	173.5
Foreign	54.9	3.2	(25.0)
Total	10.5	50.5	148.5
Total	$113.8	$347.1	$355.1

The U.K. government enacted income tax rate reductions during each of the years 2010 through 2013. During 2013, the rate was reduced from 23 percent to 21 percent effective April 2014, and to 20 percent effective April 2015. Although the rate reductions in each instance became or will become effective during a subsequent year, we are required to adjust deferred tax assets and liabilities through income on the date of enactment of a rate change. As a

result, we recorded income tax benefits of $6.3 million and $9.3 million for the tax rate reductions enacted during 2013 and 2012, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 7 - Income Tax - Continued

We consider the unremitted earnings of our foreign operations to be permanently invested and therefore have not provided U.S. deferred taxes on the cumulative earnings of our non-U.S. affiliates. Deferred taxes are provided for earnings of non-U.S. affiliates when we plan to remit those earnings. As of December 31, 2014, we have not made a provision for U.S. taxes on approximately $1 billion of the excess of the carrying amount for financial reporting over the tax basis of investments in foreign subsidiaries that are essentially permanent in duration. The determination of a deferred tax liability related to investments in these foreign subsidiaries is not practicable.

Our consolidated statements of income include the following changes in unrecognized tax benefits:

	December 31		
	2014	2013	2012
	(in millions of dollars)		
Balance at Beginning of Year	$18.4	$17.5	$86.9
Tax Positions Taken During Prior Years			
Additions	1.7	5.7	13.3
Subtractions	—	—	(0.6)
Settlements with Tax Authorities	(0.6)	(4.8)	(23.5)
Lapses of Statute of Limitations	—	—	(61.1)
Tax Positions Taken During Current Year	0.3	—	2.5
Balance at End of Year	19.8	18.4	17.5
Less Tax Attributable to Temporary Items Included Above	(10.4)	(10.2)	(15.0)
Total Unrecognized Tax Benefits that if Recognized Would Affect the Effective Tax Rate	$9.4	$8.2	$2.5

Included in the balances at December 31, 2014, 2013, and 2012 are $10.4 million, $10.2 million, and $15.0 million, respectively, of unrecognized tax benefits for tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Other than potential interest and penalties, the disallowance of the shorter deductibility period would not affect our results of operations but would accelerate the payment of cash to the taxing authority.

We recognize interest expense and penalties, if applicable, related to unrecognized tax benefits in tax expense net of federal income tax. We recognized an increase (reduction) in interest expense related to unrecognized tax benefits of $0.2 million, $(1.1) million, and $(10.4) million during 2014, 2013, and 2012, respectively. The total amounts of accrued interest and penalties related to unrecognized tax benefits in our consolidated balance sheets as of December 31, 2014 and 2013 were $1.0 million and $0.8 million, respectively. It is reasonably possible that unrecognized tax benefits could decrease within the next 12 months by up to $19.3 million as a result of resolution of audit activity with the Internal Revenue Service (IRS).

We file federal and state income tax returns in the United States and in foreign jurisdictions. We are under continuous examination by the IRS with regard to our U.S. federal income tax returns. During 2013, our appeal of tax years 2005 and 2006 was effectively settled with the approval of the Congressional Joint Committee on Taxation. As a result of the settlement, we received a cash refund of taxes and interest of $17.5 million in 2014.

During 2012, the IRS audit of our 2009 and 2010 years commenced, and we also finalized all issues with the IRS related to our 2007 and 2008 years, resulting in a reduction of our federal income taxes of $11.0 million. In the first quarter of 2015, we reached a tentative settlement of our 2009 and 2010 tax years with the IRS and expect to finalize

the settlement of these years in 2015. As part of the settlement with the IRS of the 2009 and 2010 tax years, we also resolved claims for refund we filed related to tax credits for years 2003 through 2012 and expect to record an immaterial increase in net income during 2015.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 7 - Income Tax - Continued

Tax years subsequent to 2008 remain subject to examination by tax authorities in the U.S., and tax years subsequent to 2012 remain subject to examination in major foreign jurisdictions. We believe sufficient provision has been made for all potential adjustments for years that are not closed by the statute of limitations in all major tax jurisdictions and that any such adjustments would not have a material adverse effect on our financial position, liquidity, or results of operations.

In January 2013, the American Taxpayer Relief Act retroactively reinstated the active financing income exemption to the beginning of 2012 which affects the amount of earnings from foreign subsidiaries that is taxed annually, regardless of whether foreign earnings are repatriated. Our 2012 income tax expense reflected the taxation of all active financing income from our foreign subsidiaries as required under the law in place prior to the reinstatement. In 2013, we reversed the amounts recorded in 2012 and recorded a reduction in income tax expense of $0.9 million to reflect the reinstatement of the exemption of active financing income. The active financing income exemption expired again for tax years beginning on or after January 1, 2015, the effect of which is expected to be immaterial in 2015.

As of December 31, 2014 and 2013, we had no net operating loss carryforward for U.S. income taxes. We record a valuation allowance to reduce deferred tax assets to the amount that is more likely than not to be realized. As of December 31, 2014 and 2013, we had no valuation allowance.

Total income taxes paid net of refunds during 2014, 2013, and 2012 were $155.7 million, $398.1 million, and $185.0 million, respectively.

Note 8 - Debt

Debt consists of the following:

			December 31	
			2014	2013
	Interest Rates	Maturities	(in millions of dollars)	
Long-term Debt				
Senior Secured Notes issued 2007	Variable	2037	$398.4	$440.0
Senior Notes issued 1998	7.000%	2018	200.0	200.0
Senior Notes issued 1998	6.750 - 7.250%	2028	365.8	365.8
Senior Notes issued 2002	7.375%	2032	39.5	39.5
Senior Notes issued 2005	6.850%	2015	—	296.8
Senior Notes issued 2009	7.125%	2016	350.0	350.0
Senior Notes issued 2010	5.625%	2020	399.7	399.7
Senior Notes issued 2012	5.750%	2042	248.7	248.6
Senior Notes issued 2014	4.000%	2024	349.5	—
Medium-term Notes issued 1990 - 1996	7.000 - 7.190%	2023 - 2028	50.8	50.8
Junior Subordinated Debt Securities issued 1998	7.405%	2038	226.5	226.5
Fair Value Hedges Adjustment			(0.2)	(5.7)
Total Long-term Debt			2,628.7	2,612.0
Short-term Debt				
Senior Notes issued 2005	6.850%	2015	151.9	—

Total Short-term Debt	151.9	—
Total Debt	$2,780.6	$2,612.0

The prior year amount for securities lending has been reclassified from short-term debt to other liabilities in our consolidated balance sheets to conform to the current year presentation and is therefore no longer included in the chart above. Cash flows resulting from the change in the securities lending liability in prior years have also been reclassified from financing to investing in our statements of cash flows to conform to the current year presentation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 8 - Debt - Continued

Collateralized debt is comprised of our senior secured notes and ranks highest in priority, followed by unsecured notes, which consist of senior notes and medium-term notes, followed by junior subordinated debt securities. The senior notes due 2018 and medium-term notes are non-callable and the junior subordinated debt securities are callable under limited, specified circumstances. The remaining debt is callable and may be redeemed, in whole or in part, at any time.

The aggregate contractual principal maturities are $151.9 million in 2015, $350.0 million in 2016, $200.0 million in 2018, and $2,081.0 million in 2020 and thereafter.

Senior Secured Notes

In 2007, Northwind Holdings, LLC (Northwind Holdings), a wholly-owned subsidiary of Unum Group, issued $800.0 million of insured, senior secured notes (the Northwind notes) in a private offering. The Northwind notes bear interest at a floating rate equal to the three-month LIBOR plus 0.78%.

Northwind Holdings’ ability to meet its obligations to pay principal, interest, and other amounts due on the Northwind notes will be dependent principally on its receipt of dividends from Northwind Reinsurance Company (Northwind Re), the sole subsidiary of Northwind Holdings. Northwind Re reinsured the risks attributable to specified individual disability insurance policies issued by or reinsured by Provident Life and Accident Insurance Company, Unum Life Insurance Company of America, and The Paul Revere Life Insurance Company (collectively, the ceding insurers) pursuant to separate reinsurance agreements between Northwind Re and each of the ceding insurers. The ability of Northwind Re to pay dividends to Northwind Holdings will depend on its satisfaction of applicable regulatory requirements and the performance of the reinsured policies.

Recourse for the payment of principal, interest, and other amounts due on the Northwind notes is limited to the collateral for the Northwind notes and the other assets, if any, of Northwind Holdings. The collateral consists of a first priority, perfected security interest in (a) the debt service coverage account (DSCA) that Northwind Holdings is required to maintain in accordance with the indenture pursuant to which the Northwind notes were issued (the Northwind indenture), (b) the capital stock of Northwind Re and the dividends and distributions on such capital stock, and (c) Northwind Holdings' rights under the transaction documents related to the Northwind notes to which Northwind Holdings is a party. At December 31, 2014, the amount in the DSCA was $5.4 million. None of Unum Group, the ceding insurers, Northwind Re, or any other affiliate of Northwind Holdings is an obligor or guarantor with respect to the Northwind notes.

Northwind Holdings is required to repay a portion of the outstanding principal under the Northwind notes at par on the quarterly scheduled payment dates under the Northwind notes in an amount equal to the lesser of (i) a targeted amortization amount as defined in the Northwind indenture and (ii) the amount of the remaining available funds in the DSCA minus an amount equal to the minimum balance that is required to be maintained in the DSCA under the Northwind indenture, provided that Northwind Holdings has sufficient funds available to pay its other expenses, including interest payments on the Northwind notes, and to maintain the minimum balance in the DSCA as required under the Northwind indenture. Northwind Holdings made principal payments on the Northwind notes of $41.6 million in 2014 and $60.0 million in both 2013 and 2012.

In 2006, Tailwind Holdings, LLC (Tailwind Holdings) a wholly-owned subsidiary of Unum Group, issued $130.0 million of insured, senior, secured notes due 2036 in a private offering. During 2012, Tailwind Holdings made

principal payments of $10.0 million on these notes. In 2013, we purchased and retired the outstanding principal of $62.5 million on these notes, resulting in a before-tax gain of $4.0 million.

Unsecured Notes

In May 2014, we purchased and retired $145.0 million principal of our outstanding 6.85% notes, including a make-whole amount of $13.2 million, for a total cost of $158.2 million. In conjunction with this retirement, we reclassified $13.1 million of the deferred gain on previously terminated derivatives associated with the hedge of this debt from accumulated other comprehensive income to realized investment gain in our consolidated statements of income. These notes were issued by UnumProvident Finance Company plc, a wholly-owned subsidiary of Unum Group, and the outstanding balance is fully and unconditionally guaranteed by Unum Group.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 8 - Debt - Continued

Fair Value Hedges

As of December 31, 2014 and 2013, we had $600.0 million notional amount interest rate swaps which effectively convert certain of our unsecured senior notes into floating rate debt. Under these agreements, we receive fixed rates of interest and pay variable rates of interest, based off of three-month LIBOR. See Note 4 for further information on our interest rate swaps.

Junior Subordinated Debt Securities

In 1998, Provident Financing Trust I (the trust), a 100 percent-owned finance subsidiary of Unum Group, issued $300.0 million of 7.405% capital securities in a public offering. These capital securities are fully and unconditionally guaranteed by Unum Group, have a liquidation value of $1,000 per capital security, and have a mandatory redemption feature under certain circumstances. Unum Group issued 7.405% junior subordinated deferrable interest debentures to the trust in connection with the capital securities offering. The debentures mature in 2038. The sole assets of the trust are the junior subordinated debt securities.

Interest Paid

Interest paid on long-term and short-term debt and related securities during 2014, 2013, and 2012 was $145.9 million, $144.6 million, and $139.6 million, respectively.

Credit Facility

In August 2013, we entered into a five-year, $400.0 million unsecured revolving credit facility. Under the terms of the agreement, we may request that the credit facility be increased up to $600.0 million. Borrowings under the credit facility are for general corporate uses and are subject to financial covenants, negative covenants, and events of default that are customary. The credit facility provides for borrowing at an interest rate based either on the prime rate or LIBOR. In addition, the credit facility provides for the issuance of letters of credit subject to certain terms and limitations. At December 31, 2014, letters of credit totaling $2.1 million had been issued from the credit facility. No letters of credit had been issued from the credit facility at December 31, 2013. At December 31, 2014 and 2013, there were no borrowed amounts outstanding from the credit facility.

Note 9 - Employee Benefit Plans

Defined Benefit Pension and Other Postretirement Benefit (OPEB) Plans

We sponsor several defined benefit pension and OPEB plans for our employees, including non-qualified pension plans. The U.S. qualified and non-qualified defined benefit pension plans comprise the majority of our total benefit obligation and benefit cost. We maintain a separate defined benefit plan for eligible employees in our U.K. operation. The U.S. defined benefit pension plans were closed to new entrants on December 31, 2013, and the U.K. plan was closed to new entrants on December 31, 2002.

Amendments to U.S. Pension Plans

In 2014, we amended our U.S. qualified defined benefit pension plan to allow a limited-time offer of benefit payouts to eligible former employees with a vested right to a pension benefit. The offer provided eligible former employees, regardless of age, with an option to elect to receive a lump-sum settlement of his or her entire accrued pension benefit in December 2014 or to elect receipt of monthly pension benefits commencing in January 2015. For those who elected to receive lump-sum settlements, we made payments totaling $214.5 million from plan assets in December 2014. We recognized a before-tax settlement loss of $64.4 million in earnings during 2014, with a corresponding reduction in the unrecognized actuarial loss included in accumulated other comprehensive income that pertained to the settled benefit obligation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

In 2013, we adopted plan amendments which froze participation and benefit accruals in our U.S. qualified and non-qualified defined benefit pension plans, effective December 31, 2013. Because the amendments eliminated all future service accruals subsequent to December 31, 2013 for active participants in these plans, we were required to remeasure the benefit obligations during 2013. The discount rate assumption increased from 4.50 percent at December 31, 2012 to 5.00 percent at the remeasurement date, reflecting the change in market interest rates during that period. The expected long-term rate of return on plan assets of 7.50 percent remained unchanged from December 31, 2012. The remeasurement resulted in a decrease in our net pension liability of $327.4 million at the remeasurement date, with a corresponding increase in other comprehensive income, less applicable income tax of $114.6 million. The decrease in the net pension liability resulted primarily from the curtailment of benefits under the plan amendments as well as the increase in the discount rate assumption used to remeasure the benefit obligations. As a result of the 2013 plan amendments, we recognized a before-tax curtailment loss of $0.7 million in earnings during 2013, with a corresponding reduction in the prior service cost included in accumulated other comprehensive income and associated with years of service no longer expected to be rendered.

Amendments to U.K. Pension Plan

In 2013, we adopted amendments to our U.K. pension plan which froze participation in our plan and which reduced the maximum rate of inflation indexation from 5.0 percent to 2.5 percent for pension benefits which were earned prior to April 1997. The amendment to reduce the maximum rate of inflation indexation was effective September 12, 2013, and the amendment to freeze participation became effective June 30, 2014. Although all future service accruals were eliminated for active participants, pension payments to participants currently employed are based on the higher of (i) pensionable earnings at a participant's retirement age or the date a participant's employment ceases, subject to the inflation indexation provisions in the plan, or (ii) pensionable earnings as of June 30, 2014, also subject to the inflation indexation provisions. Because the amendments eliminated all future service accruals subsequent to June 30, 2014 for active participants in the plan, we were required to remeasure the benefit obligation of the plan during 2013. The discount rate assumption increased from 4.50 percent at December 31, 2012 to 4.60 percent at the remeasurement date, reflecting the change in market interest rates during that period. The expected long-term rate of return on plan assets changed from 6.20 percent at December 31, 2012 to 6.35 percent at the remeasurement date. The remeasurement resulted in a $2.3 million, or £1.5 million, increase in our net pension asset at the remeasurement date. As a result of these plan amendments, we recognized a before-tax curtailment gain of $3.7 million, or £2.3 million, in earnings during 2013, with a corresponding decrease in the prior service credit included in accumulated other comprehensive income and associated with years of service no longer expected to be rendered. The majority of the prior service credit was related to the amendment to reduce the rate of inflation indexation.

Amendments to OPEB Plan

We discontinued offering retiree life insurance to future retirees effective December 31, 2012 but continue to provide this benefit to employees who retired prior to that date. As a result of this plan amendment, we recognized a curtailment gain of $4.2 million and a prior service credit of $5.0 million in accumulated other comprehensive income during 2012.

Amortization Period of Actuarial Gain or Loss

Because all participants in the U.S. and U.K. pension plans are considered inactive as a result of the 2013 plan amendments, we are required to amortize the net actuarial loss for these plans over the average remaining life

expectancy of the plan participants. As of December 31, 2014, the estimate of the average remaining life expectancy of plan participants was approximately 35 years for U.S. participants and 34 years for U.K. participants.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

The following tables provide the changes in the benefit obligation and fair value of plan assets and statements of the funded status of the plans.

	Pension Benefits					
	U.S. Plans		U.K. Plan		OPEB	
	2014	2013	2014	2013	2014	2013
	(in millions of dollars)					
Change in Benefit Obligation						
Benefit Obligation at Beginning of Year	$1,718.7	$1,967.9	$208.7	$197.4	$165.3	$198.8
Service Cost	3.7	59.4	2.3	4.3	0.3	0.7
Interest Cost	89.9	86.3	9.1	8.6	7.9	8.0
Plan Participant Contributions	—	—	—	—	4.1	3.9
Actuarial (Gain) Loss	343.5	(225.9)	25.2	2.6	12.9	(30.2)
Benefits and Expenses Paid	(48.7)	(42.2)	(4.3)	(4.1)	(16.6)	(15.9)
Curtailment	—	(126.8)	—	(3.7)	—	—
Settlements	(214.5)	—	—	—	—	—
Change in Foreign Exchange Rates	—	—	(14.1)	3.6	—	—
Benefit Obligation at End of Year	$1,892.6	$1,718.7	$226.9	$208.7	$173.9	$165.3
Accumulated Benefit Obligation at December 31	$1,892.6	$1,718.7	$215.3	$197.7	N/A	N/A
Change in Fair Value of Plan Assets						
Fair Value of Plan Assets at Beginning of Year	$1,590.7	$1,353.6	$225.7	$205.6	$11.4	$11.5
Actual Return on Plan Assets	140.9	224.6	37.8	15.6	0.4	0.2
Employer Contributions	5.3	54.7	2.3	4.0	12.0	11.7
Plan Participant Contributions	—	—	—	—	4.1	3.9
Benefits and Expenses Paid	(48.7)	(42.2)	(4.3)	(4.1)	(16.6)	(15.9)
Settlements	(214.5)	—	—	—	—	—
Change in Foreign Exchange Rates	—	—	(15.2)	4.6	—	—
Fair Value of Plan Assets at End of Year	$1,473.7	$1,590.7	$246.3	$225.7	$11.3	$11.4
Underfunded (Overfunded) Status	$418.9	$128.0	$(19.4)	$(17.0)	$162.6	$153.9

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

The amounts recognized in our consolidated balance sheets for our pension and OPEB plans at December 31, 2014 and 2013 are as follows.

	Pension Benefits					
	U.S. Plans		U.K. Plan		OPEB	
	2014	2013	2014	2013	2014	2013
	(in millions of dollars)					
Current Liability	$5.4	$5.2	$—	$—	$13.7	$14.6
Noncurrent Liability	413.5	136.2	—	—	148.9	139.3
Noncurrent Asset	—	(13.4)	(19.4)	(17.0)	—	—
Underfunded (Overfunded) Status	$418.9	$128.0	$(19.4)	$(17.0)	$162.6	$153.9
Unrecognized Pension and Postretirement Benefit Costs						
Net Actuarial Gain (Loss)	$(593.0)	$(342.1)	$(35.4)	$(36.9)	$(2.6)	$10.3
Prior Service Credit	—	—	—	—	0.7	2.4
	(593.0)	(342.1)	(35.4)	(36.9)	(1.9)	12.7
Deferred Income Tax Asset	207.5	119.7	10.4	10.9	10.9	5.8
Total Included in Accumulated Other Comprehensive Income (Loss)	$(385.5)	$(222.4)	$(25.0)	$(26.0)	$9.0	$18.5

The following table provides the changes recognized in other comprehensive income for the years ended December 31, 2014 and 2013.

	Pension Benefits					
	U.S. Plans		U.K. Plan		OPEB	
	2014	2013	2014	2013	2014	2013
	(in millions of dollars)					
Accumulated Other Comprehensive Income (Loss) at Beginning of Year	$(222.4)	$(549.9)	$(26.0)	$(27.0)	$18.5	$2.4
Net Actuarial Gain (Loss)						
Amortization	5.2	31.7	0.4	1.2	—	—
Curtailment	—	126.8	—	—	—	—
Settlements	64.4	—	—	—	—	—
All Other Changes	(320.5)	344.8	1.1	(0.2)	(12.9)	29.6
Prior Service Credit (Cost)						
Amortization	—	(0.1)	—	—	(1.7)	(4.9)
Curtailment	—	0.7	—	(3.7)	—	—
Plan Amendment	—	—	—	3.9	—	—
Change in Deferred Income Tax Asset	87.8	(176.4)	(0.5)	(0.2)	5.1	(8.6)
Accumulated Other Comprehensive Income (Loss) at End of Year	$(385.5)	$(222.4)	$(25.0)	$(26.0)	$9.0	$18.5

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

Plan Assets

The objective of our U.S. pension and OPEB plans is to maximize long-term return, within acceptable risk levels, in a manner that is consistent with the fiduciary standards of the Employee Retirement Income Security Act (ERISA), while maintaining sufficient liquidity to pay current benefits and expenses.

During 2014, we modified our target allocation for invested asset classes for our U.S. qualified defined benefit pension plan to add opportunistic credit and real estate asset classes. The opportunistic credit asset class consists of investments in funds that hold varied fixed income investments purchased at depressed values with the intention to later sell those investments for a gain. The real estate asset class consists primarily of commercial real estate investments. The international equity funds may allocate a certain percentage of assets to forward currency contracts. The fixed income securities include U.S. government and agency asset-backed securities, corporate investment-grade bonds, private placement securities, and bonds issued by states or other municipalities. Alternative investments utilize proprietary strategies that are intended to have a low correlation to the U.S. stock market. Prohibited investments include, but are not limited to, unlisted securities, futures contracts, options, short sales, and investments in securities issued by Unum Group or its affiliates. The invested asset classes, asset types, and benchmark indices for our U.S. qualified defined benefit pension plan is as follows. We target approximately 35 percent to equity securities, 40 percent to fixed income securities, and 25 percent to opportunistic credit, alternative, and real estate investments.

Asset Class	Asset Type	Benchmark Indices
Equity Securities	Collective fund; Individual holdings	Standard & Poor's 400 and 500 Midcap; Russell 2000 Value and Growth; Morgan Stanley Capital International (MSCI) All Country World Excluding U.S.; MSCI Europe Australasia Far East; and MSCI Emerging Markets
Fixed Income; Opportunistic Credits	Collective fund; Individual holdings	Custom Index
Alternative Investments (Hedge and Private Equity)	Fund of funds; Direct investments	Hedge Fund Research Institute Fund of Funds; Russell 2000
Real Estate	Collective fund	National Council of Real Estate Investment Fund Open-end Diversified Core Equity Index

Assets for our U.K. pension plan are primarily invested in a pooled diversified growth fund. This fund invests in assets such as global equities, hedge funds, commodities, below-investment-grade fixed income securities, and currencies. The objectives of the fund are to generate capital appreciation over the course of a complete economic and market cycle and to deliver equity-like returns in the medium-to-long term while maintaining approximately two thirds of the volatility of equity markets. Performance of this fund is measured against the U.K. inflation rate plus four percent. The remaining assets in the U.K. plan are invested in leveraged interest rate and inflation swap funds of varying durations designed to broadly match the interest rate and inflation sensitivities of the plan's liabilities. The current target allocation for the assets is 75 percent diversified growth assets and 25 percent interest rate and inflation swap funds. There are no categories of investments that are specifically prohibited by the U.K. plan, but there are general guidelines that ensure prudent investment action is taken. Such guidelines include the prevention of the plan from using derivatives for speculative purposes and limiting the concentration of risk in any one type of investment.

Assets for the OPEB plan are invested in life insurance contracts issued by one of our insurance subsidiaries. The assets support life insurance benefits payable to certain former retirees covered under the OPEB plan. The terms of

these contracts are consistent in all material respects with those the subsidiary offers to unaffiliated parties that are similarly situated. There are no categories of investments specifically prohibited by the OPEB plan.

We believe our investment portfolios are well diversified by asset class and sector, with no potential risk concentrations in any one category.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

The categorization of fair value measurements by input level for the invested assets in our U.S. pension plans is as follows:

	December 31, 2014 Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1) (in millions of dollars)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Invested Assets				
Equity Securities:				
U.S. Large Cap	$—	$181.4	$—	$181.4
U.S. Mid Cap	—	88.3	—	88.3
U.S. Small Cap	118.7	—	—	118.7
International	71.0	63.5	—	134.5
Emerging Markets	—	40.0	—	40.0
Fixed Income Securities:				
U.S. Government and Agencies	243.5	14.6	—	258.1
Corporate	1.6	321.2	—	322.8
State and Municipal Securities	—	2.9	—	2.9
Opportunistic Credits	62.8	85.0	—	147.8
Alternative Investments:				
Private Equity Direct Investments	—	—	17.2	17.2
Private Equity Funds of Funds	—	—	34.9	34.9
Hedge Funds of Funds	—	—	70.0	70.0
Cash Equivalents	52.8	—	—	52.8
Total Invested Assets	$550.4	$796.9	$122.1	$1,469.4

	December 31, 2013 Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1) (in millions of dollars)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Invested Assets				
Equity Securities:				
U.S. Large Cap	$—	$343.9	$—	$343.9
U.S. Mid Cap	—	139.6	—	139.6
U.S. Small Cap	231.9	—	—	231.9
International	134.5	131.7	—	266.2
Emerging Markets	—	76.3	—	76.3
Fixed Income Securities:				
U.S. Government and Agencies	105.7	7.4	—	113.1
Corporate	97.8	172.6	—	270.4

State and Municipal Securities	—	12.9	—	12.9
Alternative Investments:				
Private Equity Direct Investments	—	—	7.2	7.2
Private Equity Funds of Funds	—	—	29.6	29.6
Hedge Funds of Funds	—	—	66.9	66.9
Cash Equivalents	28.4	—	—	28.4
Total Invested Assets	$598.3	$884.4	$103.7	$1,586.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

Level 1 equity, fixed income, and opportunistic credit securities consist of individual holdings and funds that are valued based on unadjusted quoted prices from active markets for identical securities. Level 2 equity and opportunistic credit securities consist of funds that are valued based on the net asset value (NAV) of the underlying holdings. These investments have no unfunded commitments and no specific redemption restrictions. Level 2 fixed income securities are valued using observable inputs through market corroborated pricing.

Alternative investments, which include private equity direct investments, private equity funds of funds, and hedge funds of funds, are valued based on the NAV of the underlying holdings in a period ranging from one month to one quarter in arrears. We evaluate the need for adjustments to the NAV based on market conditions and discussions with fund managers in the period subsequent to the valuation date and prior to issuance of the financial statements. We made no adjustments to the NAV for 2014 or 2013. The private equity direct investments and private equity funds of funds generally cannot be redeemed by investors, and distributions are received following the maturity of the underlying assets. It is estimated that these underlying assets will begin to mature between five and eight years from the date of initial investment. We have assigned a Level 3 classification to the private equity direct investments and private equity funds of funds due to the redemption restrictions on the investments. Redemptions on the hedge funds of funds can be made on either a quarterly or bi-annual basis, depending on the fund, with prior notice of at least 90 calendar days. Because of these redemption restrictions, we have classified the hedge funds of funds as Level 3.

Changes in our U.S. pension plans' assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the years ended December 31, 2014 and 2013 are as follows:

	Year Ended December 31, 2014							
	Beginning of Year	Actual Return on Plan Assets Held at Year End	Actual Return on Plan Assets Sold During the Year	Purchases	Sales	Level 3 Transfers Into	Level 3 Transfers Out of	End of Year
	(in millions of dollars)							
Private Equity Direct Investments	$7.2	$1.7	$0.1	$9.0	$(0.8)	$—	$—	$17.2
Private Equity Funds of Funds	29.6	4.8	2.6	3.9	(6.0)	—	—	34.9
Hedge Funds of Funds	66.9	3.2	(0.1)	25.9	(25.9)	—	—	70.0
Total	$103.7	$9.7	$2.6	$38.8	$(32.7)	$—	$—	$122.1

	Year Ended December 31, 2013							
	Beginning of Year	Actual Return on Plan Assets Held at Year End	Actual Return on Plan Assets Sold During the Year	Purchases	Sales	Level 3 Transfers Into	Level 3 Transfers Out of	End of Year
	(in millions of dollars)							
Private Equity Direct Investments	$—	$0.3	$—	$8.4	$(1.5)	$—	$—	$7.2
Private Equity Funds of Funds	28.7	0.9	1.1	2.1	(3.2)	—	—	29.6
Hedge Funds of Funds	56.1	6.3	—	4.9	(0.4)	—	—	66.9
Total	$84.8	$7.5	$1.1	$15.4	$(5.1)	$—	$—	$103.7

146

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

The categorization of fair value measurements by input level for the assets in our U.K. pension plan is as follows.

	December 31, 2014 Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(in millions of dollars)			
Plan Assets				
Diversified Growth Assets	$—	$167.6	$—	$167.6
Fixed Interest and Index-linked Securities	78.0	—	—	78.0
Cash Equivalents	0.7	—	—	0.7
Total Plan Assets	$78.7	$167.6	$—	$246.3

	December 31, 2013 Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(in millions of dollars)			
Plan Assets				
Diversified Growth Assets	$—	$172.0	$—	$172.0
Fixed Interest and Index-linked Securities	52.6	0.4	—	53.0
Cash Equivalents	0.7	—	—	0.7
Total Plan Assets	$53.3	$172.4	$—	$225.7

Level 1 fixed interest and index-linked securities consist of individual funds that are valued based on unadjusted quoted prices from active markets for identical securities. Level 2 assets consist of funds that are valued based on the NAV of the underlying holdings. These investments have no unfunded commitments and no specific redemption restrictions.

The categorization of fair value measurements by input level for the assets in our OPEB plan is as follows:

	December 31, 2014 Quoted Prices in Active Markets for Identical Assets or Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(in millions of dollars)			
Assets				
Life Insurance Contracts	$—	$—	$11.3	$11.3

	December 31, 2013 Quoted Prices in Active Markets	Significant Other Observable	Significant Unobservable	Total

	for Identical Assets or Liabilities (Level 1)	Inputs (Level 2)	Inputs (Level 3)	
	(in millions of dollars)			
Assets				
Life Insurance Contracts	$—	$—	$11.4	$11.4

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

The fair value is represented by the actuarial present value of future cash flows of the contracts.

Changes in our OPEB plan assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the years ended December 31, 2014 and 2013 are as follows:

	Year Ended December 31, 2014				
	Beginning of Year	Actual Return on Plan Assets	Contributions	Net Benefits and Expenses Paid	End of Year
	(in millions of dollars)				
Life Insurance Contracts	$11.4	$0.4	$16.1	$(16.6)	$11.3
	Year Ended December 31, 2013				
	Beginning of Year	Actual Return on Plan Assets	Contributions	Net Benefits and Expenses Paid	End of Year
	(in millions of dollars)				
Life Insurance Contracts	$11.5	$0.2	$15.6	$(15.9)	$11.4

For the years end December 31, 2014 and 2013, the actual return on plan assets relates solely to investments still held at the reporting date. There were no transfers into or out of Level 3 during 2014 or 2013.

Measurement Assumptions

We use a December 31 measurement date for each of our plans. The weighted average assumptions used in the measurement of our benefit obligations as of December 31 and our net periodic benefit costs for the years ended December 31 are as follows:

	Pension Benefits											
	U.S. Plans				U.K. Plan				OPEB			
	2014		2013		2014		2013		2014		2013	
Benefit Obligations												
Discount Rate	4.40	%	5.30	%	3.60	%	4.40	%	4.30	%	5.00	%
Rate of Compensation Increase	N/A		4.00	%	3.60	%	3.90	%	N/A		N/A	
Net Periodic Benefit Cost												
Discount Rate	5.30	%	4.50% / 5.00%*		4.40	%	4.50% / 4.60%**		5.00	%	4.20	%
Expected Return on Plan Assets	7.50	%	7.50	%	6.10	%	6.20% / 6.35%**		5.75	%	5.75	%
Rate of Compensation Increase	N/A		4.00	%	3.90	%	3.75	%	N/A		N/A	

*In conjunction with the remeasurement due to the 2013 plan amendment, a discount rate of 4.50% was used for the period January 1, 2013 through the date of remeasurement, and a discount rate of 5.00% was used for the period subsequent to the date of remeasurement through December 31, 2013.

**In conjunction with the remeasurement due to the 2013 plan amendment, a discount rate of 4.50% and expected return on plan assets of 6.20% were used for the period January 1, 2013 through the date of remeasurement, and a

discount rate of 4.60% and expected return on plan assets of 6.35% were used for the period subsequent to the date of remeasurement through December 31, 2013.

We set the discount rate assumption annually for each of our retirement-related benefit plans at the measurement date to reflect the yield on a portfolio of high quality fixed income corporate debt instruments matched against the projected cash flows for future benefits.

Our long-term rate of return on plan assets assumption is an estimate, based on statistical analysis, of the average annual assumed return that will be produced from the plan assets until current benefits are paid. The market-related value equals the fair value of assets, determined as of the measurement date. Our expectations for the future investment returns of the asset categories are based on a combination of historical market performance, evaluations of investment forecasts obtained from external consultants and economists, and current market yields. The methodology underlying the return assumption includes the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

various elements of the expected return for each asset class such as long-term rates of return, volatility of returns, and the correlation of returns between various asset classes. The expected return for the total portfolio is calculated based on the plan's strategic asset allocation. Investment risk is measured and monitored on an ongoing basis through annual liability measurements, periodic asset/liability studies, and quarterly investment portfolio reviews. Risk tolerance is established through consideration of plan liabilities, plan funded status, and corporate financial condition.

Our mortality rate assumption reflects our best estimate, as of the measurement date, of the life expectancies of plan participants in order to determine the expected length of time for benefit payments. We derive our assumptions from industry mortality tables. The Society of Actuaries released updated mortality tables during the fourth quarter of 2014 which show that longevity in the United States is increasing, thereby establishing a new benchmark for mortality rates of private pension plan participants in the United States. Our mortality assumptions for our U.S. plans reflect the updated mortality tables. These updated tables did not impact the calculation of the benefit obligation for our U.K. defined benefit pension plan.

The expected return assumption for the life insurance reserve for our OPEB plan at December 31, 2014 and 2013 is 5.75 percent, which is based on full investment in fixed income securities with an average book yield of 5.46 percent and 5.58 percent in 2014 and 2013, respectively.

Our rate of compensation increase assumption is generally based on periodic studies of compensation trends.

At December 31, 2014 and 2013, the annual rate of increase in the per capita cost of covered postretirement health care benefits assumed for the next calendar year is 7.50 percent for each year for benefits payable to both retirees prior to Medicare eligibility as well as Medicare eligible retirees. The rate is assumed to change gradually to 5.00 percent by 2020 for measurement at December 31, 2014 and remain at that level thereafter.

The medical and dental premiums used to determine the per retiree employer subsidy are capped. Certain of the current retirees and all future retirees are subject to the cap.

Net Periodic Benefit Cost

The following table provides the components of the net periodic benefit cost for the plans described above for the years ended December 31.

	Pension Benefits								
	U.S. Plans			U.K. Plan			OPEB		
	2014	2013	2012	2014	2013	2012	2014	2013	2012
	(in millions of dollars)								
Service Cost	$3.7	$59.4	$48.8	$2.3	$4.3	$4.2	$0.3	$0.7	$1.6
Interest Cost	89.9	86.3	84.4	9.1	8.6	8.5	7.9	8.0	9.6
Expected Return on Plan Assets	(117.8)	(105.5)	(88.8)	(13.7)	(12.5)	(11.1)	(0.7)	(0.6)	(0.7)
Amortization of:									
Net Actuarial Loss	5.2	31.7	45.9	0.4	1.2	0.5	—	—	—
Prior Service Credit	—	(0.1)	(0.4)	—	—	—	(1.7)	(4.9)	(2.6)
Curtailment	—	0.7	—	—	(3.7)	—	—	—	—
Settlement	64.4	—	—	—	—	—	—	—	—
Total Net Periodic Benefit Cost	$45.4	$72.5	$89.9	$(1.9)	$(2.1)	$2.1	$5.8	$3.2	$7.9

A one percent increase or decrease in the assumed health care cost trend rate at December 31, 2014 would have increased (decreased) the service cost and interest cost by $0.1 million and $(0.1) million, respectively, and the postretirement benefit obligation by $4.7 million and $(3.4) million, respectively.

The unrecognized net actuarial loss included in accumulated other comprehensive income and expected to be amortized and included in net periodic pension cost for our pension plans during 2015 is $11.9 million before tax.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

Benefit Payments

The following table provides expected benefit payments, which reflect expected future service, as appropriate.

	Pension Benefits				
	U.S. Plans	U.K. Plan	OPEB		
	(in millions of dollars)				
Year			Gross	Subsidy Payments	Net
2015	$49.8	$5.5	$15.9	$1.9	$14.0
2016	54.1	6.0	15.6	2.1	13.5
2017	58.2	6.2	15.3	2.3	13.0
2018	62.6	6.4	14.9	2.4	12.5
2019	67.0	7.0	14.6	2.7	11.9
2020-2024	409.6	39.4	65.4	15.5	49.9

Funding Policy

The funding policy for our U.S. qualified defined benefit plan is to contribute annually an amount at least equal to the minimum annual contribution required under ERISA and other applicable laws, but generally not greater than the maximum amount that can be deducted for federal income tax purposes. We had no regulatory contribution requirements for our U.S. qualified defined benefit plan in 2014 and made no voluntary contributions during 2014. We do not expect to make any contributions in 2015. The funding policy for our U.S. non-qualified defined benefit pension plan is to contribute the amount of the benefit payments made during the year. Our expected return on plan assets and discount rate will not affect the cash contributions we are required to make to our U.S. pension and OPEB plans because we have met all minimum funding requirements required under ERISA.

We made required contributions to our U.K. plan of $2.3 million, or approximately £1.4 million, during 2014. Effective October 1, 2013, we increased contributions to our U.K. plan from 24.8 percent to 30.0 percent of pensionable earnings for plan participants. We do not expect to make any contributions in 2015, either voluntary or those required to meet the minimum funding requirements under U.K. legislation.

Our OPEB plan represents a non-vested, non-guaranteed obligation, and current regulations do not require specific funding levels for these benefits, which are comprised of retiree life, medical, and dental benefits. It is our practice to use general assets to pay medical and dental claims as they come due in lieu of utilizing plan assets for the medical and dental benefit portions of our OPEB plan.

Defined Contribution Plans

We offer a 401(k) plan to all eligible U.S. employees under which a portion of employee contributions is matched. Effective January 1, 2014, we began matching dollar-for-dollar up to 5.0 percent of base salary and any recognized sales and performance-based incentive compensation for employee contributions into the plan. Also effective January 1, 2014, we began making an additional non-elective contribution of 4.5 percent of earnings for all eligible employees and a separate transition contribution for eligible employees who met certain age and years of service criteria as of December 31, 2013. Prior to January 1, 2014, we matched dollar-for-dollar up to 3.0 percent of base salary and $0.50 on the dollar for each of the next 2.0 percent of base salary for employee contributions into the plan. The 401(k) plan

remains in compliance with ERISA guidelines and continues to qualify for a “safe harbor” from annual discrimination testing.

We also offer a defined contribution plan to all eligible U.K. employees under which a portion of employee contributions is matched. Effective July 1, 2014, we increased benefits under the defined contribution plan wherein we match two pounds for every one pound on the first 1.0 percent of employee contributions into the plan and match additional employee contributions pound-for-pound up to 5.0 percent of base salary. We previously matched pound-for-pound up to 5.0 percent of base salary for employee contributions into the defined contribution plan and made an additional non-elective contribution of 5.0 percent of base salary. Also effective July 1, 2014, we increased the non-elective contribution to 6.0 percent of base salary for all eligible employees, and a separate transition contribution is made for all eligible employees through March 31, 2016.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 9 - Employee Benefit Plans - Continued

During the years ended December 31, 2014, 2013, and 2012, we recognized costs of $76.0 million, $18.8 million, and $18.9 million, respectively, for our U.S. defined contribution plan and $5.0 million, $2.9 million, and $2.9 million, respectively, for our U.K. defined contribution plan.

Note 10 - Stockholders' Equity and Earnings Per Common Share

Earnings Per Common Share

Net income per common share is determined as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars, except share data)		
Numerator			
Net Income	$413.4	$858.1	$894.4
Denominator (000s)			
Weighted Average Common Shares - Basic	255,525.9	264,725.8	281,355.9
Dilution for Assumed Exercises of Stock Options and Nonvested Stock Awards	1,126.9	1,223.4	400.9
Weighted Average Common Shares - Assuming Dilution	256,652.8	265,949.2	281,756.8
Net Income Per Common Share			
Basic	$1.62	$3.24	$3.18
Assuming Dilution	$1.61	$3.23	$3.17

We use the treasury stock method to account for the effect of outstanding stock options, nonvested restricted stock units, and nonvested performance share units on the computation of diluted earnings per share. Under this method, these potential common shares will each have a dilutive effect, as individually measured, when the average market price of Unum Group common stock during the period exceeds the exercise price of the stock options and the grant price of the nonvested restricted stock units and the nonvested performance share units. The outstanding stock options have exercise prices ranging from $11.37 to $26.29; the nonvested restricted stock units have grant prices ranging from $19.38 to $35.47; and the nonvested performance share units have grant prices ranging from $23.97 to $33.86. See Note 11.

In computing earnings per share assuming dilution, only potential common shares that are dilutive (those that reduce earnings per share) are included. Potential common shares not included in the computation of diluted earnings per share because the impact would be antidilutive, based on then current market prices, approximated 0.1 million, 0.1 million, and 2.5 million for the years ended December 31, 2014, 2013, and 2012, respectively.

Common Stock

Our board of directors has authorized the repurchase of Unum Group's common stock under the following repurchase programs:

	Share Repurchase Program Authorized During		
	December 2013	July 2012	February 2011

	(in millions of dollars)		
Authorized Repurchase Amount	$750.0	$750.0	$1,000.0
Remaining Repurchase Amount at Year End 2014	$429.5	$—	$—

The December 2013 share repurchase program has an expiration date of June 12, 2015.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 10 - Stockholders' Equity and Earnings Per Common Share - Continued

Common stock repurchases, which are classified as treasury stock until otherwise retired, were as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Shares Repurchased	8.7	11.2	23.6
Cost of Shares Repurchased (1)	$300.6	$318.6	$500.6

(1) Includes commissions of $0.1 million, $0.2 million, and $0.6 million for the years ended December 31, 2014, 2013, and 2012, respectively.

In December 2014, we retired 60.0 million shares of our treasury stock with an average total cost of $1,451.7 million.

Preferred Stock

Unum Group has 25.0 million shares of preferred stock authorized with a par value of $0.10 per share. No preferred stock has been issued to date.

Note 11 - Stock-Based Compensation

Description of Stock Plans

Under the stock incentive plan of 2012 (the 2012 Plan), up to 20 million shares of common stock are available for awards to our employees, officers, consultants, and directors. Awards may be in the form of stock options, stock appreciation rights, restricted stock, restricted stock units, performance share units, and other stock-based awards. Each full-value award, defined as any award other than a stock option or stock appreciation right, is counted as 1.76 shares. The exercise price for stock options issued cannot be less than the fair value of the underlying common stock as of the grant date. Stock options generally have a term of eight years after the date of grant and fully vest after three years. At December 31, 2014, approximately 17.05 million shares were available for future grants under the 2012 Plan.

Under the stock incentive plan of 2007 (the 2007 Plan), which was terminated in May 2012 for purposes of any further grants, up to 35 million shares of common stock were available for awards to our employees, officers, consultants, and directors. Awards could be in the form of stock options, stock appreciation rights, restricted stock, restricted stock units, performance share units, and other stock-based awards. Each full-value award, defined as any award other than a stock option or stock appreciation right, is counted as 2.7 shares. Awards granted before the termination of the 2007 Plan remain outstanding in accordance with the plan's terms. Stock options generally have a term of eight years after the date of grant and fully vest after three years.

We issue new shares of common stock for all of our stock plan vestings and exercises.

Performance Share Units (PSUs)

Activity for PSUs classified as equity is as follows:

	Shares	Weighted Average Grant Date

	(000s)	Fair Value
Outstanding at December 31, 2013	116	$25.26
Granted	166	34.72
Forfeited	(1)	34.84
Outstanding at December 31, 2014	281	30.83

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 11 - Stock-Based Compensation - Continued

During 2014 and 2013, we issued PSUs with a weighted average grant date fair value per share of $34.72 and $25.26, respectively. Vesting for the PSUs occurs at the end of a three-year period and is contingent upon our achievement of prospective company performance goals and our total shareholder return relative to a particular peer group during the three-year period. Forfeitable dividend equivalents on PSUs are accrued in the form of additional PSUs.

At December 31, 2014, we had approximately $5.2 million of unrecognized compensation cost related to PSUs that will be recognized over a weighted average period of 1.7 years. The expense and unrecognized compensation cost assume the performance goals are attained at 100 percent. Actual performance, including modification for relative total shareholder return, may result in 0 to 180 percent of the PSUs ultimately being earned. The estimated compensation expense is adjusted for actual performance experience and is recognized ratably during the service period, or remaining service period, if and when it becomes probable that the performance conditions will be satisfied. Compensation cost for PSUs subject to accelerated vesting at the date of retirement eligibility is recognized over the implicit service period.

The fair value of PSUs is estimated on the date of initial grant using the Monte-Carlo simulation model. The assumptions used to value PSUs granted during the years shown are as follows:

	Year Ended December 31			
	2014		2013	
Expected Volatility (based on historical daily stock prices)	31	%	35	%
Expected Life (equals the performance period)	3.0 years		3.0 years	
Risk Free Interest Rate (based on U.S. Treasury yields at the date of grant)	0.65	%	0.38	%

Restricted Stock Units (RSUs)

Activity for RSUs classified as equity is as follows:

	Shares (000s)	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2013	1,322	$24.35
Granted	568	33.77
Vested	(782)	25.24
Forfeited	(27)	29.07
Outstanding at December 31, 2014	1,081	28.41

During 2014, 2013, and 2012, we issued RSUs with a weighted average grant date fair value per share of $33.77, $24.68, and $22.96, respectively. RSUs vest over a one to three-year service period, beginning at the date of grant, and the compensation cost is recognized ratably during the vesting period. Forfeitable dividend equivalents on RSUs are accrued in the form of additional RSUs. Compensation cost for RSUs subject to accelerated vesting at the date of retirement eligibility is recognized over the implicit service period.

The total fair value of shares vested during 2014, 2013, and 2012 was $19.8 million, $18.3 million, and $19.5 million, respectively. At December 31, 2014, we had $10.9 million of unrecognized compensation cost related to RSUs that will be recognized over a weighted average period of 0.8 years.

153

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 11 - Stock-Based Compensation - Continued

Cash-Settled Awards

Activity for cash-settled awards classified as a liability is as follows:

	Shares (000s)	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2013	165	$24.09
Granted	46	33.85
Vested	(88)	24.47
Outstanding at December 31, 2014	123	27.31

Cash-settled awards vest over a one to three-year service period, beginning at the date of grant, and the compensation cost is recognized ratably during the vesting period. Forfeitable dividend equivalents on cash-settled awards are accrued in the form of additional units. Compensation cost for cash-settled awards subject to accelerated vesting at the date of retirement eligibility is recognized over the implicit service period.
The amount payable per unit awarded is equal to the price per share of Unum Group's common stock at settlement of the award, and as such, we measure the value of the award each reporting period based on the current stock price. The effects of changes in the stock price during the service period are recognized as compensation cost over the service period. Changes in the amount of the liability due to stock price changes after the service period are recognized as compensation cost during the period in which the changes occur.

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars, except per unit data)		
Weighted Average Grant Date Fair Value per Unit Granted	$33.85	$24.22	$23.23
Total Fair Value of Units Vested	$2.1	$2.4	$1.5
Total Fair Value of Units Paid	$2.9	$2.5	$1.5

There is no unrecognized compensation cost related to the cash-settled awards, other than future changes in the liability due to future stock price changes, as the units do not require additional future service.

Stock Options

Stock option activity is summarized as follows:

	Shares (000s)	Weighted Average Exercise Price	Remaining Contractual Term (in years)	Intrinsic Value (in millions)
Outstanding at December 31, 2013	1,395	$21.17		
Exercised	(396)	23.55		
Outstanding at December 31, 2014	999	20.23	3.8	$14.6
Exercisable at December 31, 2014	874	$19.73	3.5	$13.2

All outstanding stock options at December 31, 2014 are expected to vest. Stock options vest over a one to three-year service period, beginning at the date of grant, and the compensation cost is recognized ratably during the vesting period. Compensation cost for stock options subject to accelerated vesting at the date of retirement eligibility is

recognized over the implicit service period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 11 - Stock-Based Compensation - Continued

The intrinsic value of options exercised and fair value of options vested are as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Total Intrinsic Value of Options Exercised	$4.0	$4.4	$0.6
Total Fair Value of Options Vested	$2.4	$2.4	$2.3

At December 31, 2014, we had $0.2 million of unrecognized compensation cost related to stock options that will be recognized over a weighted average period of 0.3 years.

The fair value of stock options is estimated on the date of initial grant using the Black-Scholes valuation model. The grant date fair value and the assumptions used to value stock options granted during the years shown are as follows. There were no stock options granted in 2014.

	Year Ended December 31			
	2013		2012	
Weighted Average Grant Date Fair Value per Option	$9.77		$9.78	
Expected Volatility (based on historical daily stock prices)	52	%	52	%
Expected Life (based on historical average years to exercise)	6.0 years		6.0 years	
Expected Dividend Yield (based on the dividend rate at the date of grant)	2.14	%	1.80	%
Risk Free Interest Rate (based on U.S. Treasury yields at the date of grant)	1.12	%	1.13	%

Expense

Compensation expense for the stock plans, as reported in our consolidated statements of income, is as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Performance Share Units	$2.5	$1.1	$—
Restricted Stock Units and Cash-Settled Awards	19.0	21.0	20.9
Stock Options	0.6	1.0	2.7
Other	0.5	0.5	0.6
Total Compensation Expense, Before Income Tax	$22.6	$23.6	$24.2
Total Compensation Expense, Net of Income Tax	$14.9	$15.6	$15.6

Cash received under all share-based payment arrangements for the years ended December 31, 2014, 2013, and 2012 was $12.3 million, $11.4 million, and $4.9 million, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 12 - Reinsurance

Fourteen major companies account for approximately 92 percent of our reinsurance recoverable at December 31, 2014, and are all companies rated A or better by A.M. Best Company (AM Best) or are fully securitized by letters of credit or investment-grade fixed maturity securities held in trust. Approximately seven percent of our reinsurance recoverable relates to business reinsured either with companies rated A- or better by AM Best, with overseas entities with equivalent ratings or backed by letters of credit or trust agreements, or through reinsurance arrangements wherein we retain the assets in our general account. The remaining one percent of our reinsurance recoverable is held by companies either rated below A- by AM Best or not rated.

Reinsurance data is as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Direct Premium Income	$7,899.3	$7,777.3	$7,736.0
Reinsurance Assumed	189.8	203.2	210.9
Reinsurance Ceded	(291.9)	(355.8)	(230.8)
Net Premium Income	$7,797.2	$7,624.7	$7,716.1
Ceded Benefits and Change in Reserves for Future Benefits	$662.7	$728.7	$591.7

Note 13 - Segment Information

We have three principal operating business segments: Unum US, Unum UK, and Colonial Life. Our other segments are the Closed Block and the Corporate segments.

The Unum US segment includes group long-term and short-term disability insurance, group life and accidental death and dismemberment products, and supplemental and voluntary lines of business, which are comprised of individual disability and voluntary benefits products. These products are marketed through our field sales personnel who work in conjunction with independent brokers and consultants.

The Unum UK segment includes insurance for group long-term disability, group life, and supplemental lines of business, which include individual disability and critical illness products. Unum UK's products are sold primarily in the United Kingdom through field sales personnel and independent brokers and consultants.

The Colonial Life segment includes insurance for accident, sickness, and disability products, life products, and cancer and critical illness products marketed to employees at the workplace through an independent contractor agency sales force and brokers.

The Closed Block segment consists of individual disability, group and individual long-term care, and other insurance products no longer actively marketed. The individual disability line of business in this segment generally consists of policies we sold prior to the mid-1990s and entirely discontinued selling in 2004, other than update features contractually allowable on existing policies. We discontinued offering individual long-term care in 2009 and group long-term care in 2012. Other insurance products include group pension, individual life and corporate-owned life insurance, reinsurance pools and management operations, and other miscellaneous product lines.

The Corporate segment includes investment income on corporate assets not specifically allocated to a line of business, interest expense on corporate debt other than non-recourse debt, and certain other corporate income and expense not allocated to a line of business.

We measure and analyze our segment performance using non-GAAP financial measures. A non-GAAP financial measure is a numerical measure of a company's performance, financial position, or cash flows that excludes or includes amounts that are not normally excluded or included in the most directly comparable measure calculated and presented in accordance with GAAP. The non-GAAP financial measures of "operating revenue" and "operating income" or "operating loss" differ from total revenue and income before income tax as presented in our consolidated statements of income due to the exclusion of net realized investment gains and losses, non-operating retirement-related gains or losses, and certain other items as specified in the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 13 - Segment Information - Continued

reconciliations below. We believe operating revenue and operating income or loss are better performance measures and better indicators of the revenue and profitability and underlying trends in our business.

Realized investment gains or losses depend on market conditions and do not necessarily relate to decisions regarding the underlying business of our segments. Our investment focus is on investment income to support our insurance liabilities as opposed to the generation of realized investment gains or losses. Although we may experience realized investment gains or losses which will affect future earnings levels, a long-term focus is necessary to maintain profitability over the life of the business since our underlying business is long-term in nature, and we need to earn the interest rates assumed in calculating our liabilities.

The amortization of prior period actuarial gains or losses, a component of the net periodic benefit cost for our pensions and other postretirement benefit plans, is driven by market performance as well as plan amendments and is not indicative of the operational results of our businesses. We believe that excluding the amortization of prior period gains or losses, as well as the settlement loss from our 2014 pension plan amendment, from operating income or loss provides investors with additional information for comparison and analysis of our operating results. Although we manage our non-operating retirement-related gains or losses separately from the operational performance of our business, these gains or losses impact the overall profitability of our company and have historically increased or decreased over time, depending on plan amendments and market conditions and the resulting impact on the actuarial gains or losses in our pensions and other postretirement benefit plans.

We believe that excluding the 2014 costs related to the early retirement of debt is appropriate because in conjunction with the debt redemption, we recognized in realized investment gains and losses a deferred gain from previously terminated derivatives which were associated with the hedge of the debt. The amount recognized as a realized investment gain, which basically offsets the cost of the debt redemption, is also excluded from our non-GAAP financial measures since we analyze our performance excluding amounts reported as realized investment gains or losses. We believe it provides investors with a more realistic view of our overall profitability if we are consistent in excluding both the cost of the debt retirement as well as the gain on the hedge of the debt.

We may at other times exclude certain other items from our discussion of financial ratios and metrics in order to enhance the understanding and comparability of our operational performance and the underlying fundamentals, but this exclusion is not an indication that similar items may not recur and does not replace net income or net loss as a measure of our overall profitability.

A reconciliation of "operating revenue" to total revenue and "operating income" to income before income tax is as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Operating Revenue	$10,493.6	$10,347.0	$10,459.2
Net Realized Investment Gain	16.1	6.8	56.2
Total Revenue	$10,509.7	$10,353.8	$10,515.4
Operating Income	$1,292.5	$1,241.8	$1,239.7
Net Realized Investment Gain	16.1	6.8	56.2
Non-operating Retirement-related Loss	(70.0)	(32.9)	(46.4)

Costs Related to Early Retirement of Debt for Corporate	(13.2)	—	—
Long-term Care Reserve Increase for Closed Block	(698.2)	—	—
Unclaimed Death Benefits Reserve Increase for Unum US	—	(75.4)	—
Unclaimed Death Benefits Reserve Increase for Colonial Life	—	(20.1)	—
Group Life Waiver of Premium Benefit Reserve Reduction for Unum US	—	85.0	—
Income Before Income Tax	$527.2	$1,205.2	$1,249.5

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 13 - Segment Information - Continued

Premium income by major line of business within each of our segments is presented as follows:

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Unum US			
Group Disability			
Group Long-term Disability	$1,553.5	$1,553.9	$1,578.8
Group Short-term Disability	558.1	519.6	476.7
Group Life and Accidental Death & Dismemberment			
Group Life	1,262.3	1,213.9	1,182.1
Accidental Death & Dismemberment	125.9	121.6	115.3
Supplemental and Voluntary			
Individual Disability	466.1	465.3	477.6
Voluntary Benefits	693.8	642.8	626.0
	4,659.7	4,517.1	4,456.5
Unum UK			
Group Long-term Disability	418.9	389.9	409.7
Group Life	133.2	106.4	221.3
Supplemental	55.1	60.3	63.6
	607.2	556.6	694.6
Colonial Life			
Accident, Sickness, and Disability	759.8	738.7	724.5
Life	231.8	221.1	209.7
Cancer and Critical Illness	282.1	272.4	260.3
	1,273.7	1,232.2	1,194.5
Closed Block			
Individual Disability	624.8	687.5	736.4
Long-term Care	630.9	630.6	631.9
All Other	0.9	0.7	2.2
	1,256.6	1,318.8	1,370.5
Total	$7,797.2	$7,624.7	$7,716.1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 13 - Segment Information - Continued

Selected operating statement data by segment is presented as follows:

	Unum US	Unum UK	Colonial Life	Closed Block	Corporate	Total
	(in millions of dollars)					
Year Ended December 31, 2014						
Premium Income	$4,659.7	$607.2	$1,273.7	$1,256.6	$—	$7,797.2
Net Investment Income	890.3	151.0	146.7	1,284.1	5.3	2,477.4
Other Income	122.1	—	0.1	91.8	5.0	219.0
Operating Revenue	$5,672.1	$758.2	$1,420.5	$2,632.5	$10.3	$10,493.6
Operating Income (Loss)	$856.3	$147.8	$300.2	$122.6	$(134.4)	$1,292.5
Interest and Debt Expense Excluding Costs Related to Early Retirement of Debt	$—	$—	$—	$7.3	$147.0	$154.3
Depreciation and Amortization	$314.2	$19.2	$194.1	$5.9	$1.0	$534.4
Year Ended December 31, 2013						
Premium Income	$4,517.1	$556.6	$1,232.2	$1,318.8	$—	$7,624.7
Net Investment Income	929.6	148.5	145.4	1,272.3	(3.7)	2,492.1
Other Income	128.3	0.1	0.2	93.9	7.7	230.2
Operating Revenue	$5,575.0	$705.2	$1,377.8	$2,685.0	$4.0	$10,347.0
Operating Income (Loss)	$859.0	$132.0	$284.9	$109.4	$(143.5)	$1,241.8
Interest and Debt Expense	$0.1	$—	$—	$8.4	$140.9	$149.4
Depreciation and Amortization	$292.5	$22.5	$188.7	$5.2	$0.9	$509.8
Year Ended December 31, 2012						
Premium Income	$4,456.5	$694.6	$1,194.5	$1,370.5	$—	$7,716.1
Net Investment Income	952.3	170.8	138.6	1,230.5	23.0	2,515.2
Other Income	124.6	0.1	0.3	100.1	2.8	227.9
Operating Revenue	$5,533.4	$865.5	$1,333.4	$2,701.1	$25.8	$10,459.2
Operating Income (Loss)	$847.1	$131.3	$274.3	$95.5	$(108.5)	$1,239.7
Interest and Debt Expense	$1.1	$—	$—	$10.4	$133.9	$145.4
Depreciation and Amortization	$255.6	$27.2	$181.0	$3.9	$0.8	$468.5

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 13 - Segment Information - Continued

The following table provides the changes in deferred acquisition costs by segment:

	Unum US	Unum UK	Colonial Life	Total
	(in millions of dollars)			
Year Ended December 31, 2014				
Beginning of Year	$1,051.5	$34.3	$743.4	$1,829.2
Capitalization	292.7	10.5	220.8	524.0
Amortization	(248.1)	(12.5)	(180.2)	(440.8)
Adjustment Related to Unrealized Investment Gains	0.4	—	(9.6)	(9.2)
Foreign Currency	—	(1.9)	—	(1.9)
End of Year	$1,096.5	$30.4	$774.4	$1,901.3
Year Ended December 31, 2013				
Beginning of Year	$1,024.3	$38.8	$692.4	$1,755.5
Capitalization	252.0	9.8	205.0	466.8
Amortization	(230.0)	(14.7)	(174.2)	(418.9)
Adjustment Related to Unrealized Investment Losses	5.2	—	20.2	25.4
Foreign Currency	—	0.4	—	0.4
End of Year	$1,051.5	$34.3	$743.4	$1,829.2
Year Ended December 31, 2012				
Beginning of Year	$971.8	$40.9	$664.4	$1,677.1
Capitalization	249.2	11.8	206.3	467.3
Amortization	(196.5)	(15.7)	(166.5)	(378.7)
Adjustment Related to Unrealized Investment Gains	(0.2)	—	(11.8)	(12.0)
Foreign Currency	—	1.8	—	1.8
End of Year	$1,024.3	$38.8	$692.4	$1,755.5

Assets by segment are as follows:

	December 31	
	2014	2013
	(in millions of dollars)	
Unum US	$18,676.5	$18,384.3
Unum UK	3,702.5	3,654.1
Colonial Life	3,692.2	3,482.9
Closed Block	33,960.2	31,564.2
Corporate	2,465.7	2,318.1
Total Assets	$62,497.1	$59,403.6

Revenue is primarily derived from sources in the United States and the United Kingdom. There are no material revenues or assets attributable to foreign operations other than those reported in our Unum UK segment.

We report goodwill in our Unum US segment and in our Unum UK segment, which are the segments expected to benefit from the originating business combinations. At December 31, 2014 and 2013, goodwill was $198.7 million and $200.9 million, with $187.6 million and $189.0 million, respectively, attributable to Unum US and the remainder

attributable to Unum UK.

Stockholders' equity is allocated to the operating segments on the basis of an internal allocation formula that reflects the volume and risk components of each operating segment's business and aligns allocated equity with our target capital levels for regulatory and rating agency purposes. We modify this formula periodically to recognize changes in the views of capital requirements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 14 - Commitments and Contingent Liabilities

Commitments

We have noncancelable lease obligations on certain office space and equipment. As of December 31, 2014, the aggregate net minimum lease payments were $227.1 million payable as follows: $40.2 million in 2015, $39.6 million in 2016, $36.0 million in 2017, $18.8 million in 2018, $16.9 million in 2019, and $75.6 million thereafter. Rental expense for the years ended December 31, 2014, 2013, and 2012 was $44.2 million, $44.1 million, and $41.6 million, respectively.

At December 31, 2014, we had unfunded commitments of $238.4 million for certain of our investments. The commitments are not legally binding and may or may not be funded during the term of the investments.

Contingent Liabilities

We are a defendant in a number of litigation matters. In some of these matters, no specified amount is sought. In others, very large or indeterminate amounts, including punitive and treble damages, are asserted. There is a wide variation of pleading practice permitted in the United States courts with respect to requests for monetary damages, including some courts in which no specified amount is required and others which allow the plaintiff to state only that the amount sought is sufficient to invoke the jurisdiction of that court. Further, some jurisdictions permit plaintiffs to allege damages well in excess of reasonably possible verdicts. Based on our extensive experience and that of others in the industry with respect to litigating or resolving claims through settlement over an extended period of time, we believe that the monetary damages asserted in a lawsuit or claim bear little relation to the merits of the case, or the likely disposition value. Therefore, the specific monetary relief sought is not stated.

Unless indicated otherwise in the descriptions below, reserves have not been established for litigation and contingencies. An estimated loss is accrued when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

Claims Handling Matters

We and our insurance subsidiaries, in the ordinary course of our business, are engaged in claim litigation where disputes arise as a result of a denial or termination of benefits. Most typically these lawsuits are filed on behalf of a single claimant or policyholder, and in some of these individual actions punitive damages are sought, such as claims alleging bad faith in the handling of insurance claims. For our general claim litigation, we maintain reserves based on experience to satisfy judgments and settlements in the normal course. We expect that the ultimate liability, if any, with respect to general claim litigation, after consideration of the reserves maintained, will not be material to our consolidated financial condition. Nevertheless, given the inherent unpredictability of litigation, it is possible that an adverse outcome in certain claim litigation involving punitive damages could, from time to time, have a material adverse effect on our consolidated results of operations in a period, depending on the results of operations for the particular period.

From time to time class action allegations are pursued where the claimant or policyholder purports to represent a larger number of individuals who are similarly situated. Since each insurance claim is evaluated based on its own merits, there is rarely a single act or series of actions which can properly be addressed by a class action. Nevertheless, we monitor these cases closely and defend ourselves appropriately where these allegations are made.
Miscellaneous Matters

In October 2010, Denise Merrimon, Bobby S. Mowery, and all others similarly situated vs. Unum Life Insurance Company of America, was filed in the United States District Court for the District of Maine. This class action alleged that we breached fiduciary duties owed to certain beneficiaries under certain group life insurance policies when we paid life insurance proceeds by establishing interest-bearing retained asset accounts rather than by mailing checks. In September 2013, the District Court awarded damages to the plaintiffs based on a benchmark it created by averaging the interest rates paid on money market mutual funds and money market checking accounts. Both parties appealed to the United States Court of Appeals for the First Circuit, which overturned the District Court’s decision in July 2014, finding our payment of benefits by retained asset accounts was in full compliance with the policy terms and therefore ERISA. The United States Supreme Court denied the plaintiffs' petition for a writ of certiorari in January 2015. Thus the opinion of the Court of Appeals stands, and this case is effectively concluded.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 14 - Commitments and Contingent Liabilities - Continued

Beginning in 2011, a number of state regulators began requiring insurers to cross-check specified insurance policies with the Social Security Administration’s Death Master File to identify potential matches. If a potential match was identified, insurers were requested to determine if benefits were due, locate beneficiaries, and make payments where appropriate. We initiated this process where requested, and in 2012 we began implementing this process in all states on a forward-looking basis. In addition to implementing this on a forward-looking basis, in 2013 we began an initiative to search for potential claims from previous years. During 2013, we completed our assessment of benefits which we estimate will be paid under this initiative, and as such, established additional reserves for payment of these benefits. Similar to other insurers, we are undergoing an examination by a third party acting on behalf of a number of state treasurers concerning our compliance with the unclaimed property laws of the participating states. We are cooperating fully with this examination, as well as with a Delaware Market Conduct examination and a Voluntary Disclosure Agreement process with the state of Minnesota. The legal and regulatory environment around unclaimed death benefits continues to evolve. It is possible that the current examination and/or similar investigations by other state jurisdictions may result in additional payments to beneficiaries, the payment of abandoned funds under state law, and/or administrative penalties, the total of which may be in excess of the reserves established.

In December 2012, State of West Virginia ex rel. John D. Perdue v. Provident Life and Accident Insurance Company and State of West Virginia ex rel. John D. Perdue v. Colonial Life & Accident Insurance Company were filed in the Circuit Court of Putnam County, West Virginia. These two separate complaints alleged violations of the West Virginia Uniform Unclaimed Property Act by failing to identify and report all unclaimed insurance policy proceeds due to be escheated to West Virginia. The complaints sought to examine company records and assess penalties and costs in an undetermined amount. In December 2013, the court dismissed both complaints, holding that the West Virginia Uniform Unclaimed Property Act does not require insurance companies to periodically search the Social Security Administrations' Death Master File or escheat unclaimed life insurance benefits until a claim has been submitted. In January 2014, the plaintiff appealed the dismissal of both complaints. The appeal is now fully briefed, with oral argument set for April 2015.

In May 2013, a purported class action complaint was filed in the Superior Court of California, County of Los Angeles. The plaintiff sought to represent a class of California insureds who were issued long-term care policies containing an inflation protection feature. The plaintiff alleged we incorrectly administered the inflation protection feature, resulting in an underpayment of benefits. The complaint made allegations against us for breach of contract, bad faith, fraud, violation of Business and Professions Code 17200, and injunctive relief. We removed the case to the United States District Court for the Central District of California and filed a motion to dismiss. Rather than oppose the motion, the plaintiff filed an amended complaint, and we filed another motion to dismiss. In August 2014, the District Court dismissed the fraud claim as well as plaintiff’s requests for injunctive and declaratory relief, but granted plaintiff leave to file an amended complaint. In August 2014, the plaintiff filed a second amended purported class action complaint entitled Michael Don, Executor of The Estate of Ruben Don v. Unum Group, and Unum Life Insurance Company of America in the United States District Court for the Central District of California. The complaint alleges breach of contract, bad faith, fraud, and violation of Business and Professions Code 17200 on behalf of a nationwide class of insureds who were issued long-term care policies containing an inflation protection feature. In October 2014, we answered the second amended complaint. In December 2014, the court ordered plaintiff to show cause why he was an adequate representative with claims typical of the putative class. Briefing on those issues is complete, and we are awaiting the court’s ruling.

Summary

Various lawsuits against us, in addition to those discussed above, have arisen in the normal course of business. Further, state insurance regulatory authorities and other federal and state authorities regularly make inquiries and conduct investigations concerning our compliance with applicable insurance and other laws and regulations.

Given the complexity and scope of our litigation and regulatory matters, it is not possible to predict the ultimate outcome of all pending investigations or legal proceedings or provide reasonable estimates of potential losses, except if noted in connection with specific matters. It is possible that our results of operations or cash flows in a particular period could be materially affected by an ultimate unfavorable outcome of pending litigation or regulatory matters depending, in part, on our results of operations or cash flows for the particular period. We believe, however, that the ultimate outcome of all pending litigation and regulatory matters, after consideration of applicable reserves and rights to indemnification, should not have a material adverse effect on our financial position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 15 - Statutory Financial Information

Statutory Net Income, Capital and Surplus, and Dividends

Statutory net income for U.S. life insurance companies is reported in conformity with statutory accounting principles prescribed by the National Association of Insurance Commissioners (NAIC) and adopted by applicable domiciliary state laws. The commissioners of the states of domicile have the right to permit other specific practices that may deviate from prescribed practices. Our traditional U.S. life insurance subsidiaries have no prescribed or permitted statutory accounting practices that differ materially from statutory accounting principles prescribed by the NAIC.

Certain of our traditional U.S. life insurance subsidiaries cede blocks of business to Northwind Re, Tailwind Reinsurance Company, and Fairwind Insurance Company (Fairwind), all of which are affiliated captive reinsurance subsidiaries (captive reinsurers) domiciled in the United States, with Unum Group as the ultimate parent. These captive reinsurers were established for the limited purpose of reinsuring risks attributable to specified policies issued or reinsured by our life insurance subsidiaries. Our captive reinsurers have no material state prescribed accounting practices, except for Fairwind, which was re-domesticated from Bermuda to the state of Vermont during 2013. Vermont reporting requirements for pure captive insurance companies follow GAAP, unless the commissioner permits the use of some other basis of accounting. Fairwind has permission from Vermont to follow accounting practices that are generally consistent with current NAIC statutory accounting principles for its insurance reserves and invested assets supporting reserves. All other assets and liabilities are accounted for in accordance with GAAP, as prescribed by Vermont, which allows for the full recognition of deferred tax assets which are more likely than not to be realized. Statutory accounting principles have a stricter limitation for the recognition of deferred tax assets. The impact of following the prescribed and permitted practices of Vermont rather than statutory accounting principles prescribed by the NAIC resulted in higher capital and surplus for Fairwind of approximately $200 million and $176 million as of December 31, 2014 and 2013, respectively.

The operating results and capital and surplus of our traditional U.S. life insurance subsidiaries and our captive reinsurers, prepared in accordance with prescribed or permitted accounting practices of the NAIC or states of domicile, are presented separately below. Results for 2012 include those for Fairwind as filed with insurance regulators in Bermuda.

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Combined Net Income (Loss)			
Traditional U.S. Life Insurance Subsidiaries	$623.1	$584.5	$624.5
Captive Reinsurers	$(123.0)	$13.3	$40.8
Combined Net Gain (Loss) from Operations			
Traditional U.S. Life Insurance Subsidiaries	$618.1	$617.5	$649.8
Captive Reinsurers	$(123.8)	$13.6	$37.4

	December 31	
	2014	2013
	(in millions of dollars)	
Combined Capital and Surplus		
Traditional U.S. Life Insurance Subsidiaries	$3,462.8	$3,450.5
Captive Reinsurers	$1,668.3	$1,679.4

As derived from the most recent annual statutory basis financial statements filed with insurance regulators, the statutory net income and statutory capital and surplus of our United Kingdom insurance subsidiary, Unum Limited, were £54.6 million and £425.2 million, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 15 - Statutory Financial Information - Continued

Risk based capital (RBC) standards for U.S. life insurance companies are prescribed by the NAIC. The domiciliary states of our U.S. insurance subsidiaries have all adopted a version of the RBC model formula of the NAIC, which prescribes a system for assessing the adequacy of statutory capital and surplus for all life and health insurers. The basis of the system is a risk-based formula that applies prescribed factors to the various risk elements in a life and health insurer's business to report a minimum capital requirement proportional to the amount of risk assumed by the insurer. The life and health RBC formula is designed to measure annually (i) the risk of loss from asset defaults and asset value fluctuations, (ii) the risk of loss from adverse mortality and morbidity experience, (iii) the risk of loss from mismatching of asset and liability cash flow due to changing interest rates, and (iv) business risks. The formula is used as an early warning tool to identify companies that are potentially inadequately capitalized. State insurance laws grant insurance regulators the authority to require various actions by, or take various actions against, insurers whose total adjusted capital does not meet or exceed certain RBC levels. The total adjusted capital of each of our U.S. insurance subsidiaries at December 31, 2014 is in excess of those RBC levels.

Restrictions under applicable state insurance laws limit the amount of dividends that can be paid to a parent company from its insurance subsidiaries in any 12-month period without prior approval by regulatory authorities. For life insurance companies domiciled in the U.S., that limitation generally equals, depending on the state of domicile, either ten percent of an insurer's statutory surplus with respect to policyholders as of the preceding year end or the statutory net gain from operations, excluding realized investment gains and losses, of the preceding year. The payment of dividends to a parent company from a life insurance subsidiary is generally further limited to the amount of unassigned funds.

Based on the restrictions under current law, $604.9 million is available, without prior approval by regulatory authorities, during 2015 for the payment of dividends to Unum Group from its traditional U.S. life insurance subsidiaries. The ability of our captive insurers to pay dividends to their respective parent companies will depend on their satisfaction of applicable regulatory requirements and on the performance of the business reinsured.

We also have the ability to receive dividends from Unum Limited, subject to applicable insurance company regulations and capital guidance in the United Kingdom. Approximately £166.6 million is available for the payment of dividends from Unum Limited during 2015, subject to regulatory approval.

Deposits

At December 31, 2014 and 2013, our U.S. insurance subsidiaries had on deposit with U.S. regulatory authorities securities with a book value of $279.1 million and $280.5 million, respectively, held for the protection of policyholders.

Note 16 - Quarterly Results of Operations (Unaudited)

The following is a summary of our unaudited quarterly results of operations for 2014 and 2013:

	2014			
	4th	3rd	2nd	1st
	(in millions of dollars, except share data)			
Premium Income	$1,967.9	$1,947.2	$1,943.6	$1,938.5
Net Investment Income	629.4	606.4	629.1	612.5
Net Realized Investment Gain (Loss)	(17.3)	1.2	25.9	6.3

Total Revenue	2,635.7	2,609.4	2,653.5	2,611.1
Income (Loss) Before Income Tax	(457.9)	312.1	346.5	326.5
Net Income (Loss)	(279.1)	221.1	242.5	228.9
Net Income (Loss) Per Common Share				
Basic	(1.11)	0.87	0.94	0.88
Assuming Dilution	(1.11)	0.87	0.94	0.88

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued
Unum Group and Subsidiaries

Note 16 - Quarterly Results of Operations (Unaudited) - Continued

	2013			
	4th	3rd	2nd	1st
	(in millions of dollars, except share data)			
Premium Income	$1,890.7	$1,897.3	$1,905.8	$1,930.9
Net Investment Income	629.4	615.5	626.1	621.1
Net Realized Investment Gain (Loss)	9.3	(26.1)	13.3	10.3
Total Revenue	2,586.2	2,540.9	2,601.9	2,624.8
Income Before Income Tax	305.8	284.1	311.5	303.8
Net Income	221.2	205.7	218.6	212.6
Net Income Per Common Share				
Basic	0.85	0.78	0.82	0.79
Assuming Dilution	0.84	0.78	0.82	0.79

Items affecting the comparability of our financial results are as follows:

- Fourth quarter of 2014 reserve increase of $698.2 million before tax and $453.8 million after tax related to long-term care.
- Fourth quarter of 2014 settlement loss of $64.4 million before tax and $41.9 million after tax related to a pension plan amendment.
- Fourth quarter of 2013 reserve increase of $95.5 million before tax and $62.1 million after tax related to unclaimed death benefits.
- Fourth quarter of 2013 reserve reduction of $85.0 million before tax and $55.2 million after tax related to group life waiver of premium benefits.

See Notes 6, 9, and 14 for further discussion of the above items.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 9A. CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report. We evaluated those controls based on the 2013 Internal Control - Integrated Framework from the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, these officers concluded that our disclosure controls and procedures were effective as of December 31, 2014.

There have been no changes in our internal control over financial reporting, as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended, during the quarter ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management's Annual Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended. The Company's internal control over financial reporting encompasses the processes and procedures management has established to (i) maintain records that, in reasonable detail, accurately and fairly reflect the Company's transactions and dispositions of assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles; (iii) provide reasonable assurance that receipts and expenditures are appropriately authorized; and (iv) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. In addition, any projection of the evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We assessed the effectiveness of our internal control over financial reporting, based on criteria established in the 2013 Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and concluded that, as of December 31, 2014, we maintained effective internal control over financial reporting.

Attestation Report of the Company's Registered Public Accounting Firm

Ernst & Young LLP, the independent registered public accounting firm that audited our consolidated financial statements included herein, audited the effectiveness of our internal control over financial reporting, as of December 31, 2014, and issued the attestation report included as follows.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Unum Group

We have audited Unum Group and subsidiaries' internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). Unum Group and subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying "Management's Annual Report on Internal Control over Financial Reporting". Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

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

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Unum Group and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Unum Group and subsidiaries as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2014, and our report dated February 25, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chattanooga, Tennessee
February 25, 2015

ITEM 9B. OTHER INFORMATION

None

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Directors and Executive Officers

The information required by this Item with respect to directors is included under the caption "Information About the Board of Directors," sub-captions "Nominees for Election as Directors with Terms Expiring in 2016" and "Additional Directors," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

The information required by this Item with respect to our executive officers is included under the caption "Executive Officers of the Registrant" contained herein in Item 1 and is incorporated herein by reference.

The information required by this Item with respect to compliance with Section 16(a) of the Exchange Act is included under the caption "Ownership of Company Securities," sub-caption "Section 16(a) - Beneficial Ownership Reporting Compliance," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

The information required by this Item with respect to a code of ethics for our chief executive officer and certain senior financial officers is included under the caption "Corporate Governance," sub-caption "Codes of Conduct and Ethics," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

The information required by this Item with respect to the audit committee and audit committee financial experts is included under the caption "Corporate Governance," sub-captions "Committees of the Board" and "Audit Committee," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

Corporate Governance

Our internet website address is www.unum.com. We have adopted corporate governance guidelines, a code of conduct applicable to all of our directors, officers and employees, and charters for the audit, human capital, governance, risk and finance and regulatory compliance committees of our board of directors in accordance with the requirements of the New York Stock Exchange (NYSE). In addition, our board of directors has adopted a code of ethics applicable to our chief executive officer and certain senior financial officers in accordance with the requirements of the Securities and Exchange Commission (SEC). These documents are available free of charge on our website and in print at the request of any shareholder from the Office of the Corporate Secretary, Unum Group, 1 Fountain Square, Chattanooga, Tennessee, 37402, or by calling toll-free 1-800-718-8824. We will post on our website amendments to or waivers from any provision of our code of conduct and our code of ethics, as required by the rules and regulations of the SEC and the listing standards of the NYSE.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item with respect to executive compensation is included under the caption "Information About the Board of Directors," sub-caption "Director Compensation," and under the captions "Compensation Discussion and Analysis," "Report of the Human Capital Committee," "Compensation Tables," and "Post-Employment Compensation" in our definitive proxy statement for the 2015 Annual Meeting of Shareholders

and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item with respect to security ownership of certain beneficial owners and management is included under the caption, “Ownership of Company Securities," sub-captions "Security Ownership of Directors and Officers" and "Security Ownership of Certain Shareholders," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

Equity Compensation Plan Information

The following table gives information as of December 31, 2014 about the common stock that may be issued under all of our existing equity compensation plans.

Plan Category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted average exercise price of outstanding options, warrants and rights [5]	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity Compensation Plans Approved by Shareholders [1]	2,506,760 [3]	$20.23	18,031,864 [6]
Equity Compensation Plans Not Approved by Shareholders [2]	81,110 [4]	N/A	26,463 [7]
Total	2,587,870		18,058,327

(1) Our shareholders have approved the following plans: (a) Stock Incentive Plan of 2007, (b) Unum Group Employee Stock Purchase Plan, (c) Unum European Holding Company Limited Savings-Related Share Option Scheme 2008 (formerly the Unum Limited Savings-Related Share Option Scheme 2008), (d) Unum Ireland Savings-Related Share Option Scheme 2008, (e) Unum European Holding Company Limited Savings-Related Share Option Scheme 2011, and (f) Stock Incentive Plan of 2012.

(2) Our shareholders have not approved the Unum Group Non-Employee Director Compensation Plan of 2004.

(3) Includes 999,088 shares issuable upon the exercise of outstanding options, 1,192,241 restricted stock units, 281,298 performance share units, and 34,133 deferred share rights issuable pursuant to outstanding awards (including dividend equivalents accrued thereon), under our Stock Incentive Plan of 2007 and our Stock Incentive Plan of 2012.

(4) All are deferred share rights (each representing the right to one share of common stock), including dividend equivalents accrued thereon, granted to non-employee directors under the Unum Group Non-Employee Director Compensation Plan of 2004 in accordance with the deferral elections of such directors in respect of cash retainers and meeting fees payable to them.

(5) Restricted stock units, performance share units, and deferred share rights are not included in determining the weighted average exercise price in column (b) because they have no exercise price.

(6) Includes 75,000 shares authorized for issuance under the Unum Ireland Limited Savings-Related Share Option Scheme 2008, even though none have been reserved given that the plan is not expected to be utilized. Also includes approximately 85,971 shares available for future issuance as dividend equivalents in respect of outstanding awards under the Stock Incentive Plan of 2007, which was otherwise replaced by the Stock Incentive Plan of 2012 effective May 24, 2012 for purposes of granting new awards. As of December 31, 2014, our Stock Incentive Plan of 2012 had 17.0 million shares remaining available for future issuance. Each full-value award is counted as 1.76 shares. We currently grant a majority of awards as restricted stock units, which are full-value awards.

(7)

Represents approximate number of shares available for future issuance as dividend equivalents in respect of outstanding awards under the Non-Employee Director Compensation Plan of 2004.

Below is a brief description of the equity compensation plans not approved by shareholders:

Unum Group Amended and Restated Non-Employee Director Compensation Plan of 2004

This plan provided for the payment of annual retainers and meeting fees (discontinued in May 2011) to the non-employee directors who served on Unum Group’s board of directors. Under the plan, directors made an irrevocable election each year to receive all or a portion of their retainers and meeting fees in either cash or deferred share rights. A deferred share right is a right to receive one share of common stock on the earlier of (i) the director’s separation from service as a director of Unum Group, or (ii) another designated date at least three years after the date of the deferral election. The number of deferred share rights granted is calculated as the number of whole shares equal to (i) the dollar amount of the annual retainer and/or fees that the director elects to have paid in deferred share rights, divided by (ii) the fair market value per share on the grant date. The aggregate number of shares which can be issued under the plan is 500,000. This plan terminated in May 2010 with respect to new awards, though dividend equivalents remain available for future issuance in respect of awards that were outstanding at that time. The plan is administered by the Human Capital Committee. The plan includes provisions restricting the transferability of the deferred share rights, provisions for adjustments to the number of shares available for grants, and the number of shares subject to outstanding grants in the event of recapitalization, reclassification, stock split, reverse stock split, reorganization, merger, consolidation, or other similar corporate transaction.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information required by this Item with respect to certain relationships and related transactions and director independence is included under the caption "Corporate Governance," sub-captions "Director Independence" and "Related Party Transactions and Policy," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item with respect to fees paid to Ernst & Young LLP in 2014 and 2013 and our audit committee's pre-approval policies and procedures is included under the caption "Items to Be Voted On," sub-captions "Independent Auditor Fees" and "Policy for Pre-Approval of Audit and Non-Audit Services," in our definitive proxy statement for the 2015 Annual Meeting of Shareholders and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) List of Documents filed as part of this report: Page

(1) Financial Statements

The following report and consolidated financial statements of Unum Group and Subsidiaries are included in Item 8.

(2) Financial Statement Schedules

Schedules not referred to have been omitted as inapplicable or because they are not required by Regulation S-X.

(3) Exhibits

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Unum Group
(Registrant)
By: /s/ Thomas R. Watjen
Thomas R. Watjen
President and Chief Executive Officer
Date: February 25, 2015

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Name	Title	Date
/s/ Thomas R. Watjen Thomas R. Watjen	President and Chief Executive Officer and a Director (principal executive officer)	February 25, 2015
/s/ Richard P. McKenney Richard P. McKenney	Executive Vice President and Chief Financial Officer (principal financial officer)	February 25, 2015
/s/ Vicki W. Corbett Vicki W. Corbett	Senior Vice President, Controller (controller)	February 25, 2015

Name	Title	Date
* Theodore H. Bunting, Jr.	Director	February 25, 2015
* E. Michael Caulfield	Director	February 25, 2015
* Cynthia L. Egan	Director	February 25, 2015
* Pamela H. Godwin	Director	February 25, 2015
* Ronald E. Goldsberry	Director	February 25, 2015
* Kevin T. Kabat	Director	February 25, 2015
* Timothy F. Keaney	Director	February 25, 2015
* Thomas Kinser	Director	February 25, 2015
* Gloria C. Larson	Director	February 25, 2015
* A. S. MacMillan, Jr.	Director	February 25, 2015
* Edward J. Muhl	Director	February 25, 2015
* William J. Ryan	Director	February 25, 2015
* By: /s/ Susan N. Roth Susan N. Roth Attorney-in-Fact	For all of the Directors	February 25, 2015

SCHEDULE I--SUMMARY OF INVESTMENTS -
OTHER THAN INVESTMENTS IN RELATED PARTIES

Unum Group and Subsidiaries

Type of Investment	Cost or Amortized Cost (1)	Fair Value	Amount shown on the balance sheet	
	(in millions of dollars)			
Fixed Maturity Securities:				
Bonds				
United States Government and Government Agencies and Authorities	$983.5	$1,238.5	$1,238.5	
States, Municipalities, and Political Subdivisions	1,745.0	2,121.5	2,121.5	
Foreign Governments	1,101.1	1,307.4	1,307.4	
Public Utilities	7,046.1	8,550.6	8,550.6	
Mortgage/Asset-Backed Securities	2,224.9	2,431.8	2,431.8	
All Other Corporate Bonds	25,658.8	29,365.2	29,365.2	
Redeemable Preferred Stocks	44.0	49.9	49.9	
Total Fixed Maturity Securities	38,803.4	$45,064.9	45,064.9	
Mortgage Loans	1,856.6		1,856.6	
Policy Loans	3,306.6		3,306.6	
Other Long-term Investments				
Derivatives	—		28.0	(2)
Equity Securities	7.9		12.5	
Miscellaneous Long-term Investments	542.6		551.4	(3)
Short-term Investments	974.3		974.3	
Total Investments	$45,491.4		$51,794.3	

(1) The amortized cost for fixed maturity securities and mortgage loans represents original cost reduced by repayments, write-downs from other-than-temporary declines in fair value, amortization of premiums, and/or accretion of discounts.

(2) Derivatives are carried at fair value.

(3) The difference between amortized cost and carrying value primarily results from changes in the partnership owner's equity since acquisition.

SCHEDULE II--CONDENSED FINANCIAL INFORMATION OF REGISTRANT

Unum Group (Parent Company)

BALANCE SHEETS

	December 31	
	2014	2013
	(in millions of dollars)	
Assets		
Fixed Maturity Securities - at fair value (amortized cost: $161.4; $143.9)	$162.2	$145.3
Other Long-term Investments	51.9	57.2
Short-term Investments	326.2	164.0
Investment in Subsidiaries	10,362.7	10,082.8
Deferred Income Tax	160.1	68.1
Other Assets	568.3	558.8
Total Assets	$11,631.4	$11,076.2
Liabilities and Stockholders' Equity		
Liabilities		
Long-term Debt	$2,230.3	$1,875.2
Pension and Postretirement Benefits	581.5	295.3
Other Liabilities	267.2	246.6
Total Liabilities	3,079.0	2,417.1
Stockholders' Equity		
Common Stock	30.2	36.1
Additional Paid-in Capital	2,221.2	2,634.1
Accumulated Other Comprehensive Income	166.4	255.0
Retained Earnings	7,332.8	8,083.2
Treasury Stock	(1,198.2)	(2,349.3)
Total Stockholders' Equity	8,552.4	8,659.1
Total Liabilities and Stockholders' Equity	$11,631.4	$11,076.2

See notes to condensed financial information.

SCHEDULE II--CONDENSED FINANCIAL INFORMATION OF REGISTRANT (Continued)

Unum Group (Parent Company)

STATEMENTS OF INCOME

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Cash Dividends from Subsidiaries	$645.2	$636.6	$670.8
Other Income	116.3	56.9	55.0
Total Revenue	761.5	693.5	725.8
Interest and Debt Expense	132.4	120.9	114.2
Other Expenses	66.0	48.9	65.5
Total Expenses	198.4	169.8	179.7
Income of Parent Company Before Income Tax	563.1	523.7	546.1
Income Tax Benefit	(24.5)	(14.7)	(25.7)
Income of Parent Company	587.6	538.4	571.8
Equity in Undistributed Earnings (Loss) of Subsidiaries	(174.2)	319.7	322.6
Net Income	413.4	858.1	894.4
Other Comprehensive Income (Loss), Net of Tax	(88.6)	(373.0)	166.2
Comprehensive Income	$324.8	$485.1	$1,060.6

See notes to condensed financial information.

SCHEDULE II--CONDENSED FINANCIAL INFORMATION OF REGISTRANT (Continued)

Unum Group (Parent Company)

STATEMENTS OF CASH FLOWS

	Year Ended December 31		
	2014	2013	2012
	(in millions of dollars)		
Cash Provided by Operating Activities	$683.0	$612.5	$677.3
Cash Flows from Investing Activities			
Proceeds from Sales of Fixed Maturity Securities	25.0	—	—
Proceeds from Maturities of Fixed Maturity Securities	76.1	38.5	47.7
Proceeds from Sales and Maturities of Other Investments	31.9	9.4	1.0
Purchase of Fixed Maturity Securities	(118.9)	(139.8)	(99.1)
Purchase of Other Investments	(19.0)	(1.0)	(13.7)
Net Sales (Purchases) of Short-term Investments	(162.1)	269.5	40.4
Cash Distributions to Subsidiaries	(316.1)	(225.1)	(175.2)
Acquisition of Property and Equipment	(102.5)	(78.8)	(80.4)
Other, Net	(0.2)	(6.2)	4.2
Cash Used by Investing Activities	(585.8)	(133.5)	(275.1)
Cash Flows from Financing Activities			
Issuance of Long-term Debt	347.2	—	246.4
Issuance of Common Stock	12.3	11.4	4.9
Repurchase of Common Stock	(306.0)	(317.2)	(496.7)
Dividends Paid to Stockholders	(159.4)	(146.5)	(133.8)
Other, Net	1.9	(0.3)	1.6
Cash Used by Financing Activities	(104.0)	(452.6)	(377.6)
Increase (Decrease) in Cash	$(6.8)	$26.4	$24.6

See notes to condensed financial information.

SCHEDULE II--CONDENSED FINANCIAL INFORMATION OF REGISTRANT (Continued)

Unum Group (Parent Company)

NOTES TO CONDENSED FINANCIAL INFORMATION

Note 1 - Basis of Presentation

The accompanying condensed financial statements should be read in conjunction with the consolidated financial statements and notes thereto of Unum Group and subsidiaries.

Note 2 - Debt

Debt consists of the following:

			December 31	
			2014	2013
	Interest Rates	Maturities	(in millions of dollars)	
Long-term Debt				
Senior Notes issued 1998	7.000%	2018	$200.0	$200.0
Senior Notes issued 1998	6.750 - 7.250%	2028	365.8	365.8
Senior Notes issued 2002	7.375%	2032	39.5	39.5
Senior Notes issued 2009	7.125%	2016	350.0	350.0
Senior Notes issued 2010	5.625%	2020	399.7	399.7
Senior Notes issued 2012	5.750%	2042	248.7	248.6
Senior Notes issued 2014	4.000%	2024	349.5	—
Medium-term Notes issued 1990 - 1996	7.000 - 7.190%	2023 - 2028	50.8	50.8
Junior Subordinated Debt Securities issued 1998	7.405%	2038	226.5	226.5
Fair Value Hedges Adjustment			(0.2)	(5.7)
Total Long-term Debt			$2,230.3	$1,875.2

The prior year amount for securities lending has been reclassified from short-term debt to other liabilities in our condensed balance sheets to conform to the current year presentation and is therefore no longer included in the chart above. Cash flows resulting from the change in the securities lending liability in prior years have also been reclassified from financing to investing in our statements of cash flows to conform to the current year presentation.

The senior notes due 2018 and the medium-term notes are non-callable. The junior subordinated debt securities are callable under limited, specified circumstances. The remaining debt is callable and may be redeemed, in whole or in part, at any time. The aggregate contractual principal maturities are $350.0 million in 2016, $200.0 million in 2018, and $1,682.6 million in 2020 and thereafter.

Fair Value Hedges

As of December 31, 2014 and 2013, we had $600.0 million notional amount interest rate swaps which effectively convert certain of our unsecured senior notes into floating rate debt. Under these agreements, we receive fixed rates of interest and pay variable rates of interest, based off of the three-month London Interbank Offered Rate (LIBOR).

Junior Subordinated Debt Securities

In 1998, Provident Financing Trust I (the trust), a 100 percent-owned finance subsidiary of Unum Group, issued $300.0 million of 7.405% capital securities in a public offering. These capital securities are fully and unconditionally guaranteed by Unum Group, have a liquidation value of $1,000 per capital security, and have a mandatory redemption feature under certain circumstances. Unum Group issued 7.405% junior subordinated deferrable interest debentures to the trust in connection with the capital securities offering. The debentures mature in 2038. The sole assets of the trust are the junior subordinated debt securities.

SCHEDULE II--CONDENSED FINANCIAL INFORMATION OF REGISTRANT (Continued)

Unum Group (Parent Company)

NOTES TO CONDENSED FINANCIAL INFORMATION - CONTINUED

Interest Paid

Interest paid on long-term debt and related securities during 2014, 2013, and 2012 was $123.6 million, $116.5 million, and $109.0 million, respectively.

Credit Facility

In August 2013, we entered into a five-year, $400.0 million unsecured revolving credit facility. Under the terms of the agreement, we may request that the credit facility be increased up to $600.0 million. Borrowings under the credit facility are for general corporate uses and are subject to financial covenants, negative covenants, and events of default that are customary. The credit facility provides for borrowing at an interest rate based either on the prime rate or LIBOR. In addition, the credit facility provides for the issuance of letters of credit subject to certain terms and limitations. At December 31, 2014, letters of credit totaling $2.1 million had been issued from the credit facility. No letters of credit had been issued from the credit facility at December 31, 2013. At December 31, 2014 and 2013, there were no borrowed amounts outstanding from the credit facility.

Note 3 - Guarantees

In 2005, UnumProvident Finance Company plc, a wholly-owned subsidiary of Unum Group, issued $400.0 million of 6.85% senior debentures due 2015. As of December 31, 2014, $151.9 million of these debentures, which we fully and unconditionally guarantee, were outstanding.

SCHEDULE III--SUPPLEMENTARY INSURANCE INFORMATION

Unum Group and Subsidiaries

Segment	Deferred Acquisition Costs	Reserves for Future Policy Contract Benefits	Unearned Premiums	Policy and Contract Benefits
	(in millions of dollars)			
December 31, 2014				
Unum US	$1,096.5	$11,828.0	$46.6	$953.7
Unum UK	30.4	2,596.7	130.6	127.6
Colonial Life	774.4	1,919.7	30.8	191.4
Closed Block	—	29,585.0	188.6	256.6
Total	$1,901.3	$45,929.4	$396.6	$1,529.3
December 31, 2013				
Unum US	$1,051.5	$11,788.4	$47.6	$889.1
Unum UK	34.3	2,594.3	139.3	160.0
Colonial Life	743.4	1,815.6	30.0	193.7
Closed Block	—	26,900.8	196.9	268.2
Total	$1,829.2	$43,099.1	$413.8	$1,511.0

SCHEDULE III--SUPPLEMENTARY INSURANCE INFORMATION

Unum Group and Subsidiaries

(continued from preceding page)

Segment	Premium Income	Net Investment Income (1)	Benefits and Change in Reserves for Future Benefits (2)	Amortization of Deferred Acquisition Costs	All Other Expenses (3)	Premiums Written (4)
	(in millions of dollars)					
December 31, 2014						
Unum US	$4,659.7	$890.3	$3,288.1	$248.1	$1,279.6	$3,144.1
Unum UK	607.2	151.0	431.0	12.5	166.9	479.9
Colonial Life	1,273.7	146.7	660.6	180.2	279.5	1,042.7
Closed Block	1,256.6	1,284.1	2,931.1	—	277.0	1,248.6
Corporate	—	5.3	—	—	227.9	—
Total	$7,797.2	$2,477.4	$7,310.8	$440.8	$2,230.9	
December 31, 2013						
Unum US	$4,517.1	$929.6	$3,222.4	$230.0	$1,254.0	$3,068.0
Unum UK	556.6	148.5	413.3	14.7	145.2	448.1
Colonial Life	1,232.2	145.4	667.0	174.2	271.8	1,011.8
Closed Block	1,318.8	1,272.3	2,293.0	—	282.6	1,307.0
Corporate	—	(3.7)	—	—	180.4	—
Total	$7,624.7	$2,492.1	$6,595.7	$418.9	$2,134.0	
December 31, 2012						
Unum US	$4,456.5	$952.3	$3,238.6	$196.5	$1,251.2	$3,045.0
Unum UK	694.6	170.8	541.4	15.7	177.1	466.3
Colonial Life	1,194.5	138.6	627.3	166.5	265.3	986.3
Closed Block	1,370.5	1,230.5	2,314.9	—	290.7	1,358.6
Corporate	—	23.0	—	—	180.7	—
Total	$7,716.1	$2,515.2	$6,722.2	$378.7	$2,165.0	

(1) Net investment income is allocated based upon segmentation. Each segment has its own specifically identified assets and receives the investment income generated by those assets.

(2) Included in 2014 is a reserve charge of $698.2 million in the Closed Block segment related to our long-term care business. Included in 2013 are unclaimed death benefits reserve increases of $75.4 million in the Unum US segment and $20.1 million in the Colonial Life segment and a group life waiver of premium benefit reserve reduction of $85.0 million in the Unum US segment.

(3) Includes commissions; interest and debt expense; deferral of acquisition costs; compensation expense; non-operating retirement related loss, which in 2014 included a settlement loss of $64.4 million in the Corporate

segment related to a pension plan amendment; and other expenses. Where not directly attributable to a segment, expenses are generally allocated based on activity levels, time information, and usage statistics.

(4) Excludes life insurance.

SCHEDULE IV--REINSURANCE

Unum Group and Subsidiaries

	Gross Amount	Ceded to Other Companies	Assumed from Other Companies	Net Amount	Percentage Amount Assumed to Net	
	(in millions of dollars)					
Year Ended December 31, 2014						
Life Insurance in Force	$790,952.1	$24,416.7	$999.7	$767,535.1	0.1	%
Premium Income:						
Life Insurance	$2,056.4	$194.8	$9.6	$1,871.2	0.5	%
Accident, Health, and Other Insurance	5,842.9	97.1	180.2	5,926.0	3.0	%
Total	$7,899.3	$291.9	$189.8	$7,797.2	2.4	%
Year Ended December 31, 2013						
Life Insurance in Force	$781,495.9	$25,904.7	$1,026.2	$756,617.4	0.1	%
Premium Income:						
Life Insurance	$2,018.7	$253.6	$10.0	$1,775.1	0.6	%
Accident, Health, and Other Insurance	5,758.6	102.2	193.2	5,849.6	3.3	%
Total	$7,777.3	$355.8	$203.2	$7,624.7	2.7	%
Year Ended December 31, 2012						
Life Insurance in Force	$832,587.5	$28,658.7	$1,073.8	$805,002.6	0.1	%
Premium Income:						
Life Insurance	$1,979.1	$141.4	$10.3	$1,848.0	0.6	%
Accident, Health, and Other Insurance	5,756.9	89.4	200.6	5,868.1	3.4	%
Total	$7,736.0	$230.8	$210.9	$7,716.1	2.7	%

SCHEDULE V--VALUATION AND QUALIFYING ACCOUNTS

Unum Group and Subsidiaries

Description	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Additions Charged to Other Accounts (1)	Deductions (2)	Balance at End of Period
	(in millions of dollars)				
Year Ended December 31, 2014					
Real Estate reserve (deducted from other long-term investments)	$1.8	$0.4	$—	$1.9	$0.3
Allowance for doubtful accounts (deducted from accounts and premiums receivable)	$5.6	$1.4	$0.3	$0.9	$6.4
Year Ended December 31, 2013					
Real Estate reserve (deducted from other long-term investments)	$0.3	$1.5	$—	$—	$1.8
Allowance for doubtful accounts (deducted from accounts and premiums receivable)	$6.2	$0.7	$—	$1.3	$5.6
Year Ended December 31, 2012					
Real Estate reserve (deducted from other long-term investments)	$0.3	$—	$—	$—	$0.3
Allowance for doubtful accounts (deducted from accounts and premiums receivable)	$5.7	$0.9	$—	$0.4	$6.2

(1) Additions charged to other accounts are comprised of amounts related to fluctuations in the foreign currency exchange rate.

(2) Deductions include amounts deemed to reduce exposure of probable losses and amounts deemed uncollectible.

See Note 3 of the “Notes to Consolidated Financial Statements" contained herein in Item 8 for discussion of the mortgage loan valuation allowance.

INDEX TO EXHIBITS

With regard to applicable cross-references in this report, our current, quarterly and annual reports dated on or after May 1, 2003 are filed with the Securities and Exchange Commission (SEC) under File No. 1-11294 and such reports dated prior to May 1, 2003 are filed with the SEC under File No. 1-11834, except as otherwise noted below. Our registration statements have the file numbers noted wherever such statements are identified below.

(2.1) Asset Purchase Agreement between RBC Life Insurance Company and Provident Life and Accident Insurance Company dated November 18, 2003 (incorporated by reference to Exhibit 2.1 of our Form 10-K for the fiscal year ended December 31, 2003).

(2.2) Transition Services Agreement between RBC Life Insurance Company and Provident Life and Accident Insurance Company and UnumProvident Corporation dated November 18, 2003 (incorporated by reference to Exhibit 2.2 of our Form 10-K for the fiscal year ended December 31, 2003).

(2.3) TSA Amending Agreement between RBC Life Insurance Company and Provident Life and Accident Insurance Company and UnumProvident Corporation dated April 30, 2004 (incorporated by reference to Exhibit 2.3 of our Form 10-K for the fiscal year ended December 31, 2008).

(2.4) TSA Amending Agreement No. 2 between RBC Life Insurance Company and Provident Life and Accident Insurance Company and UnumProvident Corporation dated May 31, 2006 (incorporated by reference to Exhibit 2.4 of our Form 10-K for the fiscal year ended December 31, 2008).

(2.5) TSA Amending Agreement No. 3 between RBC Life Insurance Company and Provident Life and Accident Insurance Company and Unum Group dated October 1, 2008 (incorporated by reference to Exhibit 2.5 of our Form 10-K for the fiscal year ended December 31, 2008).

(3.1) Amended and Restated Certificate of Incorporation of Unum Group, effective May 23, 2013 (incorporated by reference to Exhibit 3.1 of our Form 8-K filed on May 24, 2013).

(3.2) Amended and Restated Bylaws of Unum Group, effective December 12, 2014 (incorporated by reference to Exhibit 3.1 of our Form 8-K filed on December 12, 2014).

(4.1) Indenture for Senior Debt Securities dated as of March 9, 2001 (incorporated by reference to Exhibit 4.1 of our Registration Statement on Form S-3 (Registration No. 333-100953) filed on November 1, 2002).

(4.2) Second Supplemental Indenture, dated as of June 18, 2002, between Unum Group and JPMorgan Chase Bank, as Trustee (incorporated by reference to Exhibit 4.2 of our Form 8-K filed on June 21, 2002).

(4.3) Indenture for Senior Debt Securities between Unum Group and The Bank of New York Mellon Trust Company, N.A. as Trustee dated as of September 30, 2009 (incorporated by reference to Exhibit 4.2 of our Form 8-K filed on September 30, 2009).

(4.4) Form of 7.125% Senior Note due 2016 (incorporated by reference to Exhibit 4.1 of our Form 8-K filed on September 30, 2009).

(4.5) Form of 5.625% Senior Note due 2020 (incorporated by reference to Exhibit 4.1 of our Form 8-K filed on September 15, 2010).

(4.6) Indenture for Senior Debt Securities, dated as of August 23, 2012, between Unum Group and The Bank of New York Mellon Trust Company, N.A., as Trustee (incorporated by reference to Exhibit 4.2 of our Form 8-K filed on August 23, 2012).

(4.7) Form of 5.75% Senior Note due 2042 (incorporated by reference to Exhibit 4.1 of our Form 8-K filed on August 23, 2012).

(4.8) Form of 4.000% Senior Note due 2024 (incorporated by reference to Exhibit 4.1 of our Form 8-K filed on March 14, 2014).

Certain instruments defining the rights of holders of long-term debt securities of our company and our subsidiaries are omitted pursuant to Item 601(b)(4)(iii) of Regulation S-K. We hereby undertake to furnish to the Securities and Exchange Commission, upon request, copies of any such instruments.

(10.1) Agreement between Provident Companies, Inc. and certain subsidiaries and American General Corporation and certain subsidiaries dated as of December 8, 1997 (incorporated by reference to Exhibit 10.18 of Provident

Companies Inc.'s Form 10-Q for fiscal quarter ended September 30, 1998).

(10.2)	Form of Change in Control Severance Agreement, as amended (incorporated by reference to Exhibit 10.8 of our Form 10-K for the fiscal year ended December 31, 2008). *
(10.3)	Form of Change in Control Severance Agreement, effective April 25, 2011. *
(10.4)	Form of Change in Control Severance Agreement, effective January 1, 2015. *
(10.5)	Unum Life Insurance Company of America 1996 Deferred Compensation Plan (incorporated by reference to Exhibit 10.1 of Unum Corporation's Form 10-K for the fiscal year ended December 31, 1995, File No. 1-9254). *
(10.6)	Unum Corporation Incentive Compensation Plan for Designated Executive Officers (incorporated by reference to Exhibit 10.2 of Unum Corporation's Form 10-K for fiscal year ended December 31, 1996, File No. 1-9254). *
(10.7)	Supplemental Executive Retirement Plan (incorporated by reference to Exhibit 10.4 of Unum Corporation's Registration Statement on Form S-1 dated June 18, 1986). *
(10.8)	Unum Group Supplemental Pension Plan, as amended and restated effective January 1, 2010 (incorporated by reference to Exhibit 10.6 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.9)	First Amendment to the Unum Group Supplemental Pension Plan, effective as of June 17, 2013 (incorporated by reference to Exhibit 10.7 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.10)	Second Amendment to the Unum Group Supplemental Pension Plan, effective as of December 31, 2013 (incorporated by reference to Exhibit 10.8 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.11)	Administrative Reinsurance Agreement between Provident Life and Accident Insurance Company and Reassure America Life Insurance Company dated to be effective July 1, 2000 (incorporated by reference to Exhibit 10.1 of our Form 8-K filed on March 2, 2001).
(10.12)	Unum Group Amended and Restated Non-Employee Director Compensation Plan of 2004, as amended (incorporated by reference to Exhibit 10.19 of our Form 10-K for the fiscal year ended December 31, 2008). *
(10.13)	Unum Group Senior Executive Retirement Plan, as amended and restated effective January 1, 2008 (incorporated by reference to Exhibit 10.11 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.14)	First Amendment to the Unum Group Senior Executive Retirement Plan, effective as of December 31, 2013(incorporated by reference to Exhibit 10.12 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.15)	California Settlement Agreement (incorporated by reference to Exhibit 10.1 of our Form 8-K filed on October 3, 2005).
(10.16)	Amendment to Regulatory Settlement Agreement (incorporated by reference to Exhibit 10.2 of our Form 8 K filed on October 3, 2005).
(10.17)	Second Amended and Restated Employment Agreement between Unum Group and Thomas R. Watjen dated as of December 27, 2013 (incorporated by reference to Exhibit 10.15 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.18)	Unum Group Stock Incentive Plan of 2007, as amended (incorporated by reference to Exhibit 10.26 of our Form 10-K for the fiscal year ended December 31, 2008). *
(10.19)	Form of Restricted Stock Unit Agreement with Employee, as amended, effective February 22, 2011, for awards under the Unum Group Stock Incentive Plan of 2007 (incorporated by reference to Exhibit 10.2 of our Form 10-Q filed on May 4, 2011). *
(10.20)	Form of Restricted Stock Unit Agreement with Director, as amended, for awards under the Unum Group Stock Incentive Plan of 2007 (incorporated by reference to Exhibit 10.32 of our Form 10-K for the fiscal year ended December 31, 2008). *
(10.21)	Amended and Restated Aircraft Time-Sharing Agreement between Thomas R. Watjen and Unum Group dated as of March 8, 2010 (incorporated by reference to Exhibit 10.2 of our Form 10-Q filed on May 5, 2010). *
(10.22)	Severance Pay Plan for Executive Vice Presidents (EVPs) (incorporated by reference to Exhibit 10.35 of our Form 10-K for the fiscal year ended December 31, 2008). *
(10.23)	Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Appendix A of our Definitive Proxy Statement on Schedule 14A filed on April 12, 2012). *

(10.24) Form of Restricted Stock Unit Agreement with Director for awards under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.1 of our Form 10-Q filed on November 1, 2012). *

(10.25)	Form of Restricted Stock Unit Agreement with Employee for awards under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.1 of our Form 10-Q filed on May 2, 2013). *
(10.26)	Form of Restricted Stock Unit Agreement with Employee for awards in 2014 under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.1 of our Form 10-Q filed on May 8, 2014). *
(10.27)	Form of Cash-Settled Restricted Stock Unit Agreement with Employee for awards under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.2 of our Form 10-Q filed on May 2, 2013). *
(10.28)	Form of Cash-Settled Restricted Stock Unit Agreement with Employee for awards in 2014 under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.2 of our Form 10-Q filed on May 8, 2014). *
(10.29)	Form of Nonqualified Stock Option Agreement for awards under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.3 of our Form 10-Q filed on May 2, 2013). *
(10.30)	Form of Performance Share Unit Agreement with Employee for awards under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.4 of our Form 10-Q filed on May 2, 2013). *
(10.31)	Form of Performance Share Unit Agreement with Employee for awards in 2014 under the Unum Group Stock Incentive Plan of 2012 (incorporated by reference to Exhibit 10.3 of our Form 10-Q filed on May 8, 2014). *
(10.32)	Annual Incentive Plan of Unum Group (incorporated by reference to Exhibit 10.1 of our Form 8-K filed on May 24, 2013). *
(10.33)	Unum Group Non-Qualified Defined Contribution Retirement Plan, effective January 1, 2014 (incorporated by reference to Exhibit 10.31 of our Form 10-K for the fiscal year ended December 31, 2013). *
(10.34)	Credit Agreement, dated as of August 29, 2013, among Unum Group, as Borrower, Wells Fargo Bank, National Association, as Administrative Agent, L/C Agent, Fronting Bank and Swingline Lender, JPMorgan Chase Bank, N.A. and SunTrust Bank, as Co-Syndication Agents, and the other lenders named therein (incorporated by reference to Exhibit 10.1 of our Form 8-K filed on August 30, 2013).
(10.35)	First Amendment to Credit Agreement, dated as of January 15, 2015, among Unum Group, as Borrower, the lenders party thereto, and Wells Fargo Bank, National Association, as Administrative Agent.
(10.36)	Consulting Agreement between Unum Group and Kevin P. McCarthy dated as of March 31, 2014 (incorporated by reference to Exhibit 10.4 of our Form 10-Q filed on May 8, 2014). *
(10.37)	Letter Agreement with Richard P. McKenney, dated January 30, 2015 (incorporated by reference to Exhibit 10.1 of our Form 8-K filed on February 3, 2015). *
(10.38)	Severance Agreement between Unum Group and Richard P. McKenney, dated effective as of April 1, 2015 (incorporated by reference to Exhibit 10.2 of our Form 8-K filed on February 3, 2015). *
(10.39)	Aircraft Time-Sharing Agreement between Unum Group and Richard P. McKenney, dated effective as of May 21, 2015 (incorporated by reference to Exhibit 10.3 of our Form 8-K filed on February 3, 2015). *
(11)	Statement Regarding Computation of Per Share Earnings (incorporated herein by reference to Note 10 of the "Notes to Consolidated Financial Statements").
(12)	Statement Regarding Computation of Ratio of Earnings to Fixed Charges.
(21)	Subsidiaries of the Registrant.
(23)	Consent of Independent Registered Public Accounting Firm.
(24)	Power of Attorney.
(31.1)	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
(31.2)	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
(32.1)	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
(32.2)	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
(101)	The following financial statements from Unum Group's Annual Report on Form 10-K for the year ended December 31, 2014, filed on February 25, 2015, formatted in XBRL: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of

187

Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Stockholders' Equity, (v) Consolidated Statements of Cash Flows, (vi) the Notes to Consolidated Financial Statements, (vii) Financial Statement Schedules.

---

* Management contract or compensatory plan required to be filed as an exhibit to this form pursuant to Item 15(c) of Form 10-K.