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 "Investments" contained herein and Notes 3, 4, and 5 of the "Notes to Consolidated Financial Statements" for further discussions 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, 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 increase the net unrealized loss 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 decrease the net unrealized loss, 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 the majority of our liabilities related to insurance contracts are not interest rate sensitive and we therefore have minimal exposure to policy withdrawal risk, 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 mitigate interest rate risk. 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 allows us to choose what we believe to be the most appropriate investment strategy, as well as to prepare for disadvantageous outcomes. This analysis is the precursor to our activities in derivative financial instruments. We use current and forward interest rate swaps and options on forward interest rate swaps, interest rate forward contracts, forward treasury locks, and forward contracts on specific fixed income securities to hedge interest rate risks and to match asset durations and cash flows with corresponding liabilities.

Short-term and long-term debt are not carried at fair value in our consolidated balance sheets. If we modify or replace existing short-term or long-term 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, 2009 and 2008 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, 2009 and 2008 are shown as follows:

	December 31, 2009			
	Notional		Hypothetical	
(in millions of dollars)	Amount of Derivatives	Fair Value	FV + 100 BP	Change in FV
Assets				
Fixed Maturity Securities [1]		$37,914.4	$34,930.8	$(2,983.6)
Mortgage Loans		1,402.5	1,336.4	(66.1)
Policy Loans, Net of Reinsurance Ceded		232.0	219.9	(12.1)
Liabilities				
Unrealized Adjustment to Reserves,				
Net of Reinsurance Ceded and Other [2]		$ (1,541.7)	$ 113.3	$ 1,655.0
Long-term Debt		(2,296.0)	(2,204.1)	91.9
Derivatives [1]				
Swaps	$1,615.9	$ (63.1)	$ (87.9)	$ (24.8)
Forwards	4.8	(0.4)	(0.2)	0.2
Embedded Derivative in Modified				
Coinsurance Arrangement		(117.4)	(121.5)	(4.1)

	December 31, 2008			
	Notional		Hypothetical	
(in millions of dollars)	Amount of Derivatives	Fair Value	FV + 100 BP	Change in FV
Assets				
Fixed Maturity Securities [1]		$32,134.1	$29,719.2	$(2,414.9)
Mortgage Loans		1,224.4	1,158.6	(65.8)
Policy Loans, Net of Reinsurance Ceded		255.4	242.4	(13.0)
Liabilities				
Unrealized Adjustment to Reserves,				
Net of Reinsurance Ceded and Other [2]		$ 809.8	$ 1,921.9	$ 1,112.1
Short-term Debt		(188.9)	(188.5)	0.4
Long-term Debt		(1,677.4)	(1,614.4)	63.0
Derivatives [1]				
Swaps	$2,265.8	$ 242.2	$ 156.2	$ (86.0)
Forwards	266.3	60.2	65.0	4.8
Embedded Derivative in Modified				
Coinsurance Arrangement		(360.5)	(330.3)	30.2

(1) These assets and liabilities 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 with a corresponding offsetting change reported in other comprehensive income or loss, net of deferred taxes.

(2) The adjustment to reserves and other for unrealized investment gains and losses reflects the adjustments to deferred acquisition costs and policyholder liabilities 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.

Quantitative and Qualitative Disclosures About Market Risk

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 flows analyses. Because we actively manage our investments and liabilities, actual changes could be less than those estimated above.

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 the U.K.

Assuming the pound to dollar exchange rate decreased 10 percent from the December 31, 2009 and 2008 levels, stockholders' equity as reported in U.S. dollars as of and for the periods then ended would have been lower by approximately $98.6 million and $72.8 million, respectively. Assuming the pound to dollar average exchange rate decreased 10 percent from the actual average exchange rates for 2009 and 2008, segment operating income, which excludes net realized investment gains and losses and income tax, as reported in U.S. dollars would have decreased approximately $27.1 million and $33.5 million, respectively, for the years then ended.

Dividends paid by Unum Limited are generally held at our U.K. finance subsidiary. 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 and currency forward contracts to hedge or minimize the foreign exchange risk associated with these instruments.

See "Unum UK Segment" contained herein for further information concerning foreign currency translation.

Risk Management

As an insurer, we are in the business of risk management. Effectively taking and managing risks is essential to the success of our Company. To facilitate this effort, we have an Enterprise Risk Management (ERM) program. Our ERM program strives to:

- Identify, measure, mitigate, and report on our risk positions and exposures, including notable risk events;
- Assess material risks, including how they affect us, how individual risks interrelate, and how management addresses these risks;
- Practice strong risk management, including diversification across and within business units and systematic limit monitoring;
- Identify emerging risks and analyze how material future risks might affect us; and
- Fulfill regulatory, rating agency, and governance objectives.

Through adherence to these objectives, we believe we are better positioned to fulfill our corporate mission, improve and protect stockholder value, and reduce reputational risk.

Our approach to risk management is defined by these fundamental principles:

- Our risk management strategy begins with our business strategy. We are a specialty insurance carrier focused on providing benefits through employer-sponsored plans. We have market leadership positions in the product lines we offer and more than 160 years of experience. This combination of focused expertise and deep experience is the foundation of our approach to risk management.

- Risk management cannot be successful in a vacuum; it needs to be embedded in daily decision-making throughout the organization. Unum Group's board members and our senior leaders clearly acknowledge that risk management is critical to our Company's long-term success, and this theme cascades through the work of risk committees and the management team. Additionally, we believe the individual and collective decisions of our employees play a key role in successfully managing our overall risk profile.
- We closely monitor emerging risks, adjust our strategies as appropriate, and hold capital levels which provide financial flexibility. We use qualitative and quantitative approaches to identify emerging risks and develop mitigating strategies to limit our exposure to existing and potential risks.

We utilize stress testing and scenario analysis to shape our business, financial, and strategic planning activities. For example, 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 capital and liquidity levels. In addition, scenario analysis is used as input in the development of our business and strategic planning processes.

Risk Committee Structure and Role

We have a "pyramid" risk committee structure in place to govern our ERM process.

Unum Group's board of directors has broad responsibility for risk management, with the audit committee having principal oversight of the risk management program. Our chief risk officer regularly reports to the audit committee and also to the full board of directors, as appropriate.

An 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 a corporate risk committee and by the risk committees of the three primary operating segments that comprise Unum Group.

Operating segment risk committees for Unum US, Unum UK, and Colonial Life oversee risk specific to their business. These committees are responsible for identifying, measuring, reporting, and managing insurance and operational risks within their respective areas, consistent with corporate guidance.

The corporate risk committee oversees the operational, investment, and capital management subcommittees and reviews risk on a corporate level. Market and credit risk are jointly managed by the investment committee. The capital management committee is responsible for monitoring and planning capital allocation, financing, and liquidity.

In addition to the formal communication channels included in the risk committee structure, we provide ways for employees to report risk directly to the chief risk officer, and we educate employees on Company risks.

Governance, Risk, and Compliance

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. 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.

The recent recession and financial sector problems have reinforced the importance of effective governance, risk management, and compliance. We rely on four complementary functions.

- Internal controls provide reasonable assurance that there are controls in place to prevent and detect a material misstatement in our financial reporting;
- Internal audits assess the effectiveness of controls for operational business processes and monitor compliance with internal policies and procedures;
- Our compliance organization seeks to ensure compliance with laws and regulations and is responsible for directing our ethics program and privacy efforts; and
- The ERM program serves as an umbrella and takes a holistic view of risks and risk management efforts across the enterprise.

These groups work closely together to align their plans, activities, and efforts toward the common goal of effective governance, risk, and compliance.