HANOVER INSURANCE GROUP, INC.
Form 10-Q
July 30, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2015

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

For the transition period from to

Commission File Number 1-13754

THE HANOVER INSURANCE GROUP, INC.

(Exact name of registrant as specified in its charter)

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

440 Lincoln Street, Worcester, Massachusetts 01653

(Address of principal executive offices) (Zip Code)

(508) 855-1000

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

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

The number of shares outstanding of the registrant's common stock was 44,193,261 as of July 28, 2015.

TABLE OF CONTENTS

PART I - FINANCIAL INFORMATION
ITEM 1 - FINANCIAL STATEMENTS

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

| | Three Months Ended | Six Months Ended |
|---|---|---|

| (In millions, except per share data) | June 30, 2015 | 2014 | June 30, 2015 | 2014 |
|---|---|---|---|---|
| Revenues | | | | |
| Premiums | $ 1,205.8 | $ 1,174.7 | $ 2,416.8 | $ 2,337.7 |
| Net investment income | 70.7 | 67.0 | 140.8 | 134.0 |
| Net realized investment gains (losses): | | | | |
| Net realized gains from sales and other | 14.5 | 22.3 | 26.6 | 26.7 |
| Net other–than–temporary impairment losses on investments recognized in earnings | (1.9) | (0.1) | (4.6) | (0.1) |
| Total net realized investment gains | 12.6 | 22.2 | 22.0 | 26.6 |
| Fees and other income | 8.0 | 9.1 | 16.2 | 18.6 |
| Total revenues | 1,297.1 | 1,273.0 | 2,595.8 | 2,516.9 |
| | | | | |
| Losses and expenses | | | | |
| Losses and loss adjustment expenses | 744.9 | 725.5 | 1,518.0 | 1,476.0 |
| Amortization of deferred acquisition costs | 262.0 | 259.6 | 522.6 | 513.3 |
| Interest expense | 14.9 | 16.3 | 30.8 | 32.6 |
| Gain on disposal of U.K. motor business | (37.7) | - | (37.7) | - |
| Other operating expenses | 160.4 | 163.9 | 332.5 | 315.2 |
| Total losses and expenses | 1,144.5 | 1,165.3 | 2,366.2 | 2,337.1 |
| Income before income taxes | 152.6 | 107.7 | 229.6 | 179.8 |
| | | | | |
| Income tax expense (benefit): | | | | |
| Current | 5.7 | (1.6) | 34.9 | 7.6 |
| Deferred | 26.0 | 26.8 | 18.9 | 35.0 |
| Total income tax expense | 31.7 | 25.2 | 53.8 | 42.6 |
| | | | | |
| Income from continuing operations | 120.9 | 82.5 | 175.8 | 137.2 |
| Net (loss) gain from discontinued operations (net of tax benefit of $0.1 for the three months ended June 30, 2015 and June 30, 2014 and $0.2 for the six months ended June 30, 2015 and June 30, 2014) | (0.2) | 0.1 | (0.2) | - |
| Net income | $ 120.7 | $ 82.6 | $ 175.6 | $ 137.2 |
| | | | | |
| Earnings per common share: | | | | |
| Basic: | | | | |
| Income from continuing operations | $ 2.74 | $ 1.87 | $ 3.98 | $ 3.12 |
| Net (loss) gain from discontinued operations | (0.01) | 0.01 | - | - |
| Net income per share | $ 2.73 | $ 1.88 | $ 3.98 | $ 3.12 |
| Weighted average shares outstanding | 44.2 | 44.1 | 44.2 | 44.0 |
| | | | | |
| Diluted: | | | | |
| Income from continuing operations | $ 2.69 | $ 1.84 | $ 3.90 | $ 3.06 |
| Net (loss) gain from discontinued operations | (0.01) | - | - | - |
| Net income per share | $ 2.68 | $ 1.84 | $ 3.90 | $ 3.06 |
| Weighted average shares outstanding | 45.0 | 44.9 | 45.1 | 44.8 |

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

2

Table of Contents

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

| (In millions) | Three Months Ended June 30, 2015 | 2014 | Six Months Ended June 30, 2015 | 2014 |
|---|---|---|---|---|
| Net income | $ 120.7 | $ 82.6 | $ 175.6 | $ 137.2 |
| Other comprehensive income (loss), net of tax: | | | | |
| Available-for-sale securities and derivative instruments: | | | | |
| Net (depreciation) appreciation during the period | (92.6) | 34.3 | (63.5) | 81.5 |
| Change in other-than-temporary impairment losses recognized in other comprehensive income | (2.1) | - | (4.4) | 1.6 |
| Total available-for-sale securities and derivative instruments | (94.7) | 34.3 | (67.9) | 83.1 |
| Pension and postretirement benefits: | | | | |
| Net actuarial losses and prior service costs arising in the period | (3.3) | - | (1.4) | - |
| Amortization recognized as net periodic benefit and postretirement cost | 3.4 | 1.6 | 5.1 | 3.4 |
| Total pension and postretirement benefits | 0.1 | 1.6 | 3.7 | 3.4 |
| Cumulative foreign currency translation adjustment: | | | | |
| Amount recognized as cumulative foreign currency translation during the period | 7.7 | 3.1 | (2.2) | 3.0 |
| Total other comprehensive (loss) income, net of tax | (86.9) | 39.0 | (66.4) | 89.5 |
| Comprehensive income | $ 33.8 | $ 121.6 | $ 109.2 | $ 226.7 |

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (UNAUDITED)

| (In millions, except share data) | June 30, 2015 | December 31, 2014 |
|---|---|---|
| Assets | | |
| Investments: | | |
| Fixed maturities, at fair value (amortized cost of $6,671.0 and $7,145.7) | $ 6,835.0 | $ 7,378.1 |
| Equity securities, at fair value (cost of $516.7 and $506.6) | 565.6 | 580.8 |
| Other investments | 309.3 | 291.4 |
| Total investments | 7,709.9 | 8,250.3 |
| Cash and cash equivalents (includes restricted cash of $106.1 and $2.4) | 583.7 | 373.3 |
| Accrued investment income | 62.0 | 66.9 |
| Premiums and accounts receivable, net | 1,520.5 | 1,360.9 |
| Reinsurance recoverable on paid and unpaid losses and unearned premiums | 2,822.3 | 2,268.2 |
| Deferred acquisition costs | 522.4 | 525.7 |
| Deferred income taxes | 138.0 | 131.2 |
| Goodwill | 184.2 | 184.6 |
| Other assets | 514.1 | 486.6 |
| Assets of discontinued operations | 87.6 | 112.0 |
| Total assets | $ 14,144.7 | $ 13,759.7 |
| | | |
| Liabilities | | |
| Loss and loss adjustment expense reserves | $ 6,591.3 | $ 6,391.7 |
| Unearned premiums | 2,736.7 | 2,583.9 |
| Expenses and taxes payable | 653.1 | 695.4 |
| Reinsurance premiums payable | 329.5 | 226.8 |
| Debt | 835.1 | 903.5 |
| Liabilities of discontinued operations | 90.5 | 114.4 |
| Total liabilities | 11,236.2 | 10,915.7 |
| | | |
| Commitments and contingencies | | |
| Shareholders' Equity | | |
| Preferred stock, par value $0.01 per share; 20.0 million shares authorized; none issued | - | - |
| Common stock, par value $0.01 per share; 300.0 million shares authorized; 60.5 million shares issued | 0.6 | 0.6 |
| Additional paid-in capital | 1,830.3 | 1,830.7 |
| Accumulated other comprehensive income | 140.0 | 206.4 |
| Retained earnings | 1,690.1 | 1,558.7 |
| Treasury stock at cost (16.6 million shares) | (752.5) | (752.4) |
| Total shareholders' equity | 2,908.5 | 2,844.0 |
| Total liabilities and shareholders' equity | $ 14,144.7 | $ 13,759.7 |

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (UNAUDITED)

| | Six Months Ended June 30, | |
|---|---|---|
| (In millions) | 2015 | 2014 |
| Preferred Stock | | |
| Balance at beginning and end of period | $ - | $ - |
| Common Stock | | |
| Balance at beginning and end of period | 0.6 | 0.6 |
| Additional Paid-in Capital | | |
| Balance at beginning of period | 1,830.7 | 1,830.1 |
| Employee and director stock-based awards and other | (0.4) | (5.6) |
| Balance at end of period | 1,830.3 | 1,824.5 |
| Accumulated Other Comprehensive Income (Loss), net of tax | | |
| Net Unrealized Appreciation on Investments and Derivative Instruments: | | |
| Balance at beginning of period | 300.9 | 259.3 |
| Net (depreciation) appreciation on available-for-sale securities and derivative instruments | (67.9) | 83.1 |
| Balance at end of period | 233.0 | 342.4 |
| Defined Benefit Pension and Postretirement Plans: | | |
| Balance at beginning of period | (84.3) | (76.1) |
| Net amount arising in the period | (1.4) | - |
| Net amount recognized as net periodic benefit cost | 5.1 | 3.4 |
| Balance at end of period | (80.6) | (72.7) |
| Cumulative Foreign Currency Translation Adjustment: | | |
| Balance at beginning of period | (10.2) | (5.6) |
| Amount recognized as cumulative foreign currency translation during the period | (2.2) | 3.0 |
| Balance at end of period | (12.4) | (2.6) |
| Total accumulated other comprehensive income | 140.0 | 267.1 |
| Retained Earnings | | |
| Balance at beginning of period | 1,558.7 | 1,349.1 |
| Net income | 175.6 | 137.2 |
| Dividends to shareholders | (36.3) | (32.6) |
| Stock-based compensation | (7.9) | (2.0) |
| Balance at end of period | 1,690.1 | 1,451.7 |
| Treasury Stock | | |
| Balance at beginning of period | (752.4) | (762.9) |
| Shares purchased at cost | (23.5) | (6.7) |
| Net shares reissued at cost under employee stock-based compensation plans | 23.4 | 20.8 |
| Balance at end of period | (752.5) | (748.8) |
| Total shareholders' equity | $ 2,908.5 | $ 2,795.1 |

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

Table of Contents

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

| (In millions) | Six Months Ended June 30, 2015 | | 2014 | |
|---|---|---|---|---|
| Cash Flows From Operating Activities | | | | |
| Net income | $ | 175.6 | $ | 137.2 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | | |
| Gain on disposition of U.K. motor business | | (37.7) | | - |
| Net loss on repurchase of debt | | 18.5 | | - |
| Net realized investment gains | | (21.6) | | (26.6) |
| Net amortization and depreciation | | 16.8 | | 16.9 |
| Stock-based compensation expense | | 7.5 | | 7.3 |
| Amortization of defined benefit plan costs | | 7.2 | | 5.2 |
| Deferred income taxes expense | | 18.8 | | 34.9 |
| Change in deferred acquisition costs | | (21.4) | | (34.6) |
| Change in premiums receivable, net of reinsurance premiums payable | | (98.9) | | (122.8) |
| Change in loss, loss adjustment expense and unearned premium reserves | | 329.2 | | 352.2 |
| Change in reinsurance recoverable | | (191.2) | | (69.9) |
| Change in expenses and taxes payable | | (60.3) | | (101.8) |

| | | |
|---|---|---|
| Other, net | (39.8) | (30.6) |
| Net cash provided by operating activities | 102.7 | 167.4 |
| | | |
| Cash Flows From Investing Activities | | |
| Proceeds from disposals and maturities of fixed maturities | 881.7 | 669.0 |
| Proceeds from disposals of equity securities and other investments | 230.0 | 95.3 |
| Purchase of fixed maturities | (668.8) | (583.4) |
| Purchase of equity securities and other investments | (236.0) | (196.4) |
| Cash received from disposition of U.K. motor business, net of cash transferred | 44.3 | - |
| Capital expenditures | (8.1) | (7.4) |
| Net cash provided by (used in) investing activities | 243.1 | (22.9) |
| | | |
| Cash Flows From Financing Activities | | |
| Proceeds from exercise of employee stock options | 9.3 | 6.7 |
| Change in cash collateral related to securities lending program | 2.1 | 2.0 |
| Dividends paid to shareholders | (36.3) | (32.6) |
| Repurchases of debt | (86.5) | (0.1) |
| Repurchases of common stock | (23.5) | (6.7) |
| Other financing activities | (2.3) | (2.3) |
| Net cash used in financing activities | (137.2) | (33.0) |
| Effect of exchange rate changes on cash | 1.8 | 8.5 |
| Net change in cash and cash equivalents | 210.4 | 120.0 |
| Net change in cash related to discontinued operations | - | - |

| | | | | |
|---|---|---|---|---|
| Cash and cash equivalents, beginning of period | | 373.3 | | 486.2 |
| Cash and cash equivalents, end of period | $ | 583.7 | $ | 606.2 |

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

THE HANOVER INSURANCE GROUP, INC. AND SUBSIDIARIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Basis of Presentation and Principles of Consolidation

The accompanying unaudited consolidated financial statements of The Hanover Insurance Group, Inc. and subsidiaries (“THG” or the “Company”) have been prepared in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”) for interim financial information and with the requirements of Form 10-Q. Certain financial information that is provided in annual financial statements, but is not required in interim reports, has been omitted.

The interim consolidated financial statements of THG include the accounts of The Hanover Insurance Company (“Hanover Insurance”) and Citizens Insurance Company of America, THG’s principal U.S. domiciled property and casualty companies; Chaucer Holdings Limited (“Chaucer”), a specialist insurance underwriting group which operates through the Society and Corporation of Lloyd’s (“Lloyd’s”) and certain other insurance and non-insurance subsidiaries. These legal entities conduct their operations through several business segments discussed in Note 10 – “Segment Information”. Additionally, the interim consolidated financial statements include the Company’s discontinued operations, consisting primarily of the Company’s former life insurance businesses and its accident and health business. All intercompany accounts and transactions have been eliminated.

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

In the opinion of the Company’s management, the accompanying interim consolidated financial statements reflect all adjustments, consisting of normal recurring items, necessary for a fair presentation of the financial position and results of operations. The results of operations for the three and six months ended June 30, 2015 are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the Company’s 2014 Annual Report on Form 10-K filed with the Securities and Exchange Commission (“SEC”) on February 24, 2015.

2. New Accounting Pronouncements

Recently Implemented Standards

In April 2014, the FASB issued Accounting Standards Codification (“ASC”) Update No. 2014-08, (Topic 205 and Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. This ASC update modifies the definition of discontinued operations by limiting discontinued operations reporting to disposals of components of an entity that represent strategic shifts that have (or will have) a major effect on an entity’s operations and financial results. Also, this update requires additional financial statement disclosures about discontinued operations, as well as disposals of an individually significant component of an entity that do not qualify for discontinued operations presentation. This ASC update was effective for all disposals (or classifications as held for sale) of components of an entity that occurred within annual and interim periods beginning on or after December 15, 2014 and for all businesses that, on acquisition, were classified as held for sale that also occurred within interim and annual periods beginning on or after December 15, 2014. The Company implemented this guidance effective January 1, 2015. The effect of implementing this guidance was not material to the Company’s financial position or results of operations.

Recently Issued Standards

In May 2015, the FASB issued ASC Update No. 2015-09, (Topic 944) Financial Services- Insurance: Disclosures about Short-Duration Contracts. This ASC update requires several additional disclosures regarding short-duration insurance contracts, including; disaggregated incurred and paid claims development information, quantitative and qualitative information about claim frequency and duration, and the sum of incurred but not reported (“IBNR”) liabilities plus expected development on reported claims included in the liability for unpaid claims and claim adjustment expenses along with a description of reserving methodologies. This information is required to be presented by accident year, for the number of years for which claims typically remain outstanding, but need not exceed 10 years. A reconciliation of the claims development disclosures to the aggregate carrying amount of the liability for unpaid claims and claim adjustment expenses, including a separate disclosure for reinsurance recoverables is also required for each period presented in the statement of financial position. In addition, this ASC requires insurance entities to disclose information about significant changes in methodologies and assumptions used to calculate the liability for unpaid claims and claim adjustment expenses, including reasons for the change and the effects on the financial statements. The updated guidance is effective for annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016. Early adoption is permitted. The Company does not expect the adoption of ASC Update 2015-09 to have a material impact on its financial position or results of operations, as the update is disclosure related.

Table of Contents

In April 2015, the FASB issued ASC Update No. 2015-03, (Subtopic 835-30) Interest-Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs. This ASC update requires that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of a debt liability, consistent with debt discounts or premiums, and amortization of debt issuance cost shall be reported as interest expense. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASC update. The updated guidance is to be applied on a retrospective basis and early adoption is permitted. The update is effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The Company does not expect the adoption of ASC update 2015-03 to have a material impact on its financial position or results of operations.

In May 2014, the FASB issued ASC Update No. 2014-09, (Topic 606) Revenue from Contracts with Customers. This ASC was issued to clarify the principles for recognizing revenue. Insurance Contracts and financial instrument transactions are not within the scope of this updated guidance, and; therefore, only an insignificant amount of the Company’s revenue is subject to this updated guidance. The updated guidance is effective for periods beginning after December 15, 2016 and is not expected to have a material effect on the Company’s financial position or results of operations.

In August 2014, the FASB issued ASC update No. 2014-15, (Subtopic 205-40) Presentation of Financial Statements – Going Concern. This ASC update provides guidance on determining when and how to disclose going concern uncertainties in the financial statements, and requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year of the date the financial statements are issued. The updated guidance is effective for annual periods ending after December 15, 2016 and interim periods thereafter. Early adoption is permitted. The Company does not expect the adoption of ASC update 2014-15 to have a material impact on its financial position or results of operations.

3. Disposal of U.K. Motor Business

Effective June 30, 2015, the Company transferred its U.K. motor business to an unaffiliated U.K.-based insurance provider. The transaction was executed through a 100 percent reinsurance arrangement for prior claim liabilities and in-force policies written by this division and the sale of two entities associated with this business. Total consideration from the sale of the Chaucer subsidiaries was $64.9 million and the transaction resulted in a net gain of $40.3 million.

The components of the gain are as follows:

| | | |
|---|---|---|
| (in millions) | | |
| Total consideration | $ | 64.9 |
| Less: | | |
| Carrying value of subsidiaries | | (7.6) |
| Intangibles and goodwill disposed (1) | | (17.7) |
| Transaction expenses and employee-related and other costs (2) | | (7.7) |
| Realized gain on investments transferred as part of reinsurance agreement (3) | | 5.8 |
| Pre-tax gain | | 37.7 |
| Income tax benefit | | 2.6 |
| Net gain | $ | 40.3 |

(1) Reflects $17.2 million of indefinite-lived intangible assets associated with the U.K. motor business upon THG's purchase of Chaucer in July 2011 and $0.5 million of goodwill.
(2) Transaction costs include legal, actuarial and other professional fees.
(3) As part of the reinsurance agreement, investments were transferred, resulting in the recognition of net realized investment gains that were previously reflected in accumulated other comprehensive income.

In connection with the reinsurance arrangement, insurance liabilities of approximately $443 million were ceded, including $137.4 million of written premiums, and approximately $419 million of investments, cash, and premiums receivable were transferred. The $25 million difference between assets and liabilities equals the deferred acquisition costs ("DAC") balance associated with this business; hence, this transaction resulted in no net gain or loss.

Table of Contents

4. Income Taxes

Income tax expense for the six months ended June 30, 2015 and 2014 has been computed using estimated annual effective tax rates. These rates are revised, if necessary, at the end of each successive interim period to reflect current estimates of the annual effective tax rates.

For the six months ended June 30, 2015, the tax provision is comprised of a $37.4 million U.S. federal income tax expense and a $16.4 million foreign income tax expense. For the six months ended June 30, 2014, the tax provision was comprised of a $24.7 million U.S. federal income tax expense and a $17.9 million foreign income tax expense. Income tax expense for the six months ended June 30, 2014 included a benefit of $4.4 million related to foreign exchange losses that was deductible on the Company's 2013 U.S. tax return. This permanent tax item was not otherwise recognized in the Company's U.S. GAAP financial statements.

Although most of the Company's non–U.S. income is subject to U.S. federal income tax, a portion of its non–U.S. income is not subject to U.S. federal income tax until repatriated. Foreign taxes on this non–U.S. income are accrued at the local foreign tax rate, as opposed to the higher U.S. statutory rate, since these earnings currently are expected to be indefinitely reinvested overseas. This assumption could change as a result of a sale of the subsidiaries, the receipt of dividends from the subsidiaries, a change in management's intentions, or as a result of various other events. The Company has not made a provision for U.S. taxes on $63.0 million and $5.6 million of non-U.S. income for the six months ended June 30, 2015 and 2014, respectively. However, in the future, if all such earnings were distributed to the Company, taxes of $43.2 million would be payable on all such undistributed earnings from the current and prior years and would be reflected in the tax provision for the year in which these earnings are no longer intended to be indefinitely reinvested overseas, assuming all foreign tax credits are realized.

The Company or its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state jurisdictions, as well as foreign jurisdictions. The Company and its subsidiaries are subject to U.S. federal income tax examinations by tax authorities for years after 2010, U.S. state income tax examinations for years after 2006 and foreign examinations for years after 2011.

5. Debt

Debt consists of the following:

| (in millions) | June 30, 2015 | December 31, 2014 |
|---|---|---|
| Senior debentures maturing June 15, 2021 | $ 300.0 | $ 300.0 |
| Senior debentures maturing March 1, 2020 | 102.4 | 164.6 |
| Senior debentures maturing October 15, 2025 | 74.6 | 81.1 |
| Subordinated debentures maturing March 30, 2053 | 175.0 | 175.0 |
| Subordinated debentures maturing February 3, 2027 | 59.7 | 59.7 |
| FHLBB borrowings (secured) | 125.0 | 125.0 |
| Total principal debt | $ 836.7 | $ 905.4 |
| Unamortized debt discount | (1.6) | (1.9) |
| Total | $ 835.1 | $ 903.5 |

During the first half of 2015, the Company repurchased senior debentures maturing March 1, 2020, with a carrying value of $61.5 million at a cost of $78.2 million, resulting in a loss of $16.7 million, and senior debentures maturing October 15, 2025, with a carrying value of $6.5 million at a cost of $8.3 million, resulting in a loss of $1.8 million. These losses are included in other operating expenses.

At June 30, 2015, the Company was in compliance with the covenants associated with its debt indentures and credit arrangements.

Table of Contents

6. Investments

A. Fixed maturities and equity securities

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

| | June 30, 2015 | | | | |
|---|---|---|---|---|---|
| (in millions) | Amortized Cost or Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | OTTI Unrealized Losses |
| Fixed maturities: | | | | | |
| U.S. Treasury and government agencies | $ 440.0 | $ 6.3 | $ 4.1 | $ 442.2 | $ - |
| Foreign government | 204.1 | 2.9 | 2.7 | 204.3 | - |
| Municipal | 1,071.3 | 52.8 | 5.0 | 1,119.1 | - |
| Corporate | 3,564.3 | 132.6 | 39.9 | 3,657.0 | 14.3 |
| Residential mortgage-backed | 752.7 | 17.9 | 4.0 | 766.6 | 0.3 |
| Commercial mortgage-backed | 529.9 | 9.1 | 2.0 | 537.0 | - |
| Asset-backed | 108.7 | 0.5 | 0.4 | 108.8 | - |
| Total fixed maturities | $ 6,671.0 | $ 222.1 | $ 58.1 | $ 6,835.0 | $ 14.6 |
| Equity securities | $ 516.7 | $ 54.3 | $ 5.4 | $ 565.6 | $ - |

| | December 31, 2014 | | | | |
|---|---|---|---|---|---|
| (in millions) | Amortized Cost or Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | OTTI Unrealized Losses |
| Fixed maturities: | | | | | |
| U.S. Treasury and government agencies | $ 516.3 | $ 7.6 | $ 3.5 | $ 520.4 | $ - |
| Foreign government | 349.4 | 5.2 | 0.6 | 354.0 | - |
| Municipal | 1,079.6 | 62.4 | 4.0 | 1,138.0 | - |
| Corporate | 3,746.3 | 166.3 | 31.8 | 3,880.8 | 7.4 |
| Residential mortgage-backed | 770.4 | 21.7 | 3.0 | 789.1 | 0.4 |
| Commercial mortgage-backed | 516.7 | 12.4 | 1.3 | 527.8 | - |
| Asset-backed | 167.0 | 1.2 | 0.2 | 168.0 | - |

| | | | | | |
|---|---|---|---|---|---|
| Total fixed maturities | $ 7,145.7 | $ 276.8 | $ 44.4 | $ 7,378.1 | $ 7.8 |
| Equity securities | $ 506.6 | $ 76.8 | $ 2.6 | $ 580.8 | $ - |

Other-than-temporary impairments ("OTTI") unrealized losses in the tables above represent OTTI recognized in accumulated other comprehensive income. This amount excludes net unrealized gains on impaired securities relating to changes in the value of such securities subsequent to the impairment measurement date of $11.1 million and $12.3 million as of June 30, 2015 and December 31, 2014, respectively.

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

| | June 30, 2015 | |
|---|---|---|
| (in millions) | Amortized Cost | Fair Value |
| Due in one year or less | $ 409.8 | $ 413.9 |
| Due after one year through five years | 2,168.9 | 2,243.2 |
| Due after five years through ten years | 2,127.7 | 2,167.4 |
| Due after ten years | 573.3 | 598.1 |
| | 5,279.7 | 5,422.6 |
| Mortgage-backed and asset-backed securities | 1,391.3 | 1,412.4 |
| Total fixed maturities | $ 6,671.0 | $ 6,835.0 |

Table of Contents

B. Securities in an unrealized loss position

The following tables provide information about the Company's fixed maturities and equity securities that were in an unrealized loss position at June 30, 2015 and December 31, 2014 including the length of time the securities have been in an unrealized loss position:

| | June 30, 2015 | | | | | |
|---|---|---|---|---|---|---|
| | 12 months or less | | Greater than 12 months | | Total | |
| (in millions) | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value |
| Fixed maturities: | | | | | | |
| Investment grade: | | | | | | |
| U.S. Treasury and government agencies | $ 1.3 | $ 74.1 | $ 2.8 | $ 100.8 | $ 4.1 | $ 174.9 |
| Foreign governments | 1.8 | 58.1 | 0.9 | 5.6 | 2.7 | 63.7 |
| Municipal | 2.6 | 132.1 | 2.4 | 77.8 | 5.0 | 209.9 |
| Corporate | 14.6 | 709.1 | 9.9 | 120.9 | 24.5 | 830.0 |
| Residential mortgage-backed | 2.0 | 150.7 | 2.0 | 54.0 | 4.0 | 204.7 |
| Commercial mortgage-backed | 1.8 | 187.9 | 0.2 | 17.6 | 2.0 | 205.5 |
| Asset-backed | 0.4 | 35.2 | - | 5.0 | 0.4 | 40.2 |
| Total investment grade | 24.5 | 1,347.2 | 18.2 | 381.7 | 42.7 | 1,728.9 |
| Below investment grade: | | | | | | |
| Corporate | 13.5 | 151.6 | 1.9 | 23.2 | 15.4 | 174.8 |
| Total fixed maturities | 38.0 | 1,498.8 | 20.1 | 404.9 | 58.1 | 1,903.7 |
| Equity securities | 5.4 | 151.9 | - | - | 5.4 | 151.9 |
| Total | $ 43.4 | $ 1,650.7 | $ 20.1 | $ 404.9 | $ 63.5 | $ 2,055.6 |

| | December 31, 2014 | | | | | |
|---|---|---|---|---|---|---|
| | 12 months or less | | Greater than 12 months | | Total | |
| (in millions) | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value |
| Fixed maturities: | | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Investment grade: | | | | | | |
| U.S. Treasury and government agencies | $ - | $ 52.2 | $ 3.5 | $ 137.9 | $ 3.5 | $ 190.1 |
| Foreign governments | 0.4 | 20.8 | 0.2 | 24.2 | 0.6 | 45.0 |
| Municipal | 0.3 | 57.1 | 3.7 | 140.2 | 4.0 | 197.3 |
| Corporate | 7.8 | 393.3 | 9.3 | 217.4 | 17.1 | 610.7 |
| Residential mortgage-backed | 0.2 | 36.4 | 2.8 | 98.0 | 3.0 | 134.4 |
| Commercial mortgage-backed | 0.4 | 90.4 | 0.9 | 60.8 | 1.3 | 151.2 |
| Asset-backed | 0.1 | 46.6 | 0.1 | 13.2 | 0.2 | 59.8 |
| Total investment grade | 9.2 | 696.8 | 20.5 | 691.7 | 29.7 | 1,388.5 |
| Below investment grade: | | | | | | |
| Corporate | 12.2 | 114.9 | 2.5 | 28.3 | 14.7 | 143.2 |
| Total fixed maturities | 21.4 | 811.7 | 23.0 | 720.0 | 44.4 | 1,531.7 |
| Equity securities | 2.2 | 130.2 | 0.4 | 3.9 | 2.6 | 134.1 |
| Total | $ 23.6 | $ 941.9 | $ 23.4 | $ 723.9 | $ 47.0 | $ 1,665.8 |

Table of Contents

The Company views gross unrealized losses on fixed maturities and equity securities as being temporary since it is its assessment that these securities will recover in the near term, allowing the Company to realize the anticipated long-term economic value. The Company employs a systematic methodology to evaluate declines in fair value below amortized cost for fixed maturity securities or cost for equity securities. In determining OTTI of fixed maturity and equity securities, the Company evaluates several factors and circumstances, including the issuer's overall financial condition; the issuer's credit and financial strength ratings; the issuer's financial performance, including earnings trends, dividend payments and asset quality; any specific events which may influence the operations of the issuer; the general outlook for market conditions in the industry or geographic region in which the issuer operates; and the length of time and the degree to which the fair value of an issuer's securities remains below the Company's cost. With respect to fixed maturity investments, the Company considers any factors that might raise doubt about the issuer's ability to make contractual payments as they come due and whether the Company expects to recover the entire amortized cost basis of the security. With respect to equity securities, the Company considers its ability and intent to hold the investment for a period of time to allow for a recovery in value.

C. Other investments

In accordance with Lloyd's operating guidelines, the Company deposits funds at Lloyd's to support underwriting operations. These funds are available only to fund claim obligations. These assets consisted of approximately $387 million of fixed maturities and $106 million of cash and cash equivalents as of June 30, 2015. The Company also deposits funds with various state and governmental authorities in the U.S. For a discussion of the Company's deposits with state and governmental authorities, see also Note 3 – "Investments" of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2014.

D. Proceeds from sales

The proceeds from sales of available-for-sale securities and gross realized gains and losses on those sales, were as follows:

| | Three Months Ended June 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2015 | | | 2014 | | |
| (in millions) | Proceeds from Sales | Gross Gains | Gross Losses | Proceeds from Sales | Gross Gains | Gross Losses |
| Fixed maturities | $ 594.4 | $ 10.6 | $ 1.4 | $ 70.5 | $ 1.1 | $ 1.1 |
| Equity securities | $ 83.1 | $ 7.7 | $ - | $ 60.0 | $ 22.2 | $ 0.7 |

| | Six Months Ended June 30, | |
|---|---|---|
| | 2015 | 2014 |

| (in millions) | Proceeds from Sales | Gross Gains | Gross Losses | Proceeds from Sales | Gross Gains | Gross Losses |
|---|---|---|---|---|---|---|
| Fixed maturities | $ 824.7 | $ 12.9 | $ 4.7 | $ 208.1 | $ 3.3 | $ 2.3 |
| Equity securities | $ 167.8 | $ 20.1 | $ - | $ 72.4 | $ 24.1 | $ 0.8 |

Proceeds from sales of fixed maturities for the three and six months ended June 30, 2015 included proceeds of $379.6 million from the transfer of fixed maturity investments in connection with the sale and reinsurance of the U.K. motor business and related gross gains of $6.4 million and gross losses of $0.6 million.

E. Other-than-temporary impairments

For the three months ended June 30, 2015, total OTTI of fixed maturities was $5.1 million. Of this amount, $1.9 million was recognized in earnings and the remaining $3.2 million was recorded as unrealized losses in accumulated other comprehensive income. For the six months ended June 30, 2015, total OTTI of fixed maturities and equity securities were $11.4 million. Of this amount, $4.6 million was recognized in earnings and the remaining $6.8 million was recorded as unrealized losses in accumulated other comprehensive income.

For the three and six months ended June 30, 2014, OTTI of fixed maturities recognized in earnings was $0.1 million, which was transferred from unrealized losses in accumulated other comprehensive income.

The methodology and significant inputs used to measure the amount of credit losses on fixed maturities in 2015 were as follows:

Corporate bonds – the Company utilized a financial model that derives expected cash flows based on probability-of-default factors by credit rating and asset duration and loss-given-default factors based on security type. These factors are based on historical data provided by an independent third-party rating agency.

Table of Contents

The following table provides rollforwards of the cumulative amounts related to the Company's credit loss portion of the OTTI losses on fixed maturity securities for which the non-credit portion of the loss is included in other comprehensive income.

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (in millions) | 2015 | 2014 | 2015 | 2014 |
| Credit losses at beginning of period | $ 4.5 | $ 5.3 | $ 4.2 | $ 7.8 |
| Credit losses for which an OTTI was not previously recognized | 1.7 | - | 2.7 | - |
| Reductions for securities sold, matured or called | (0.1) | (0.6) | (0.8) | (3.1) |
| Reductions for securities reclassified as intended to sell | - | (0.4) | - | (0.4) |
| Credit losses at end of period | $ 6.1 | $ 4.3 | $ 6.1 | $ 4.3 |

7. Fair Value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability, i.e., exit price, in an orderly transaction between market participants. The Company emphasizes the use of observable market data whenever available in determining fair value. Fair values presented for certain financial instruments are estimates which, in many cases, may differ significantly from the amounts that could be realized upon immediate liquidation. A hierarchy of the three broad levels of fair value are as follows, with the highest priority given to Level 1 as these are the most observable, and the lowest priority given to Level 3:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 – Quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data, including model-derived valuations.

Level 3 – Unobservable inputs that are supported by little or no market activity.

When more than one level of input is used to determine fair value, the financial instrument is classified as Level 2 or 3 according to the lowest level input that has a significant impact on the fair value measurement.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments and have not changed since last year.

Cash and Cash Equivalents

The carrying amount approximates fair value. Cash equivalents primarily consist of money market instruments, which are generally valued using unadjusted quoted prices in active markets that are accessible for identical assets and are classified as Level 1.

Fixed Maturities

Level 1 securities generally include U.S. Treasury issues and other securities that are highly liquid and for which quoted market prices are available. Level 2 securities are valued using pricing for similar securities and pricing models that incorporate observable inputs including, but not limited to yield curves and issuer spreads. Level 3 securities include issues for which little observable data can be obtained, primarily due to the illiquid nature of the securities, and for which significant inputs used to determine fair value are based on the Company's own assumptions. Non-binding broker quotes are also included in Level 3.

The Company utilizes a third party pricing service for the valuation of the majority of its fixed maturity securities and receives one quote per security. When quoted market prices in an active market are available, they are provided by the pricing service as the fair value and such values are classified as Level 1. Since fixed maturities other than U.S. Treasury securities generally do not trade on a daily basis, the pricing service prepares estimates of fair value for those securities using pricing applications based on a market approach. Inputs into the fair value pricing common to all asset classes include: benchmark U.S. Treasury security yield curves; reported trades of identical or similar fixed maturity securities; broker/dealer quotes of identical or similar fixed maturity securities and structural characteristics such as maturity date, coupon, mandatory principal payment dates, frequency of interest and principal payments, and optional redemption features. Inputs into the fair value applications that are unique by asset class include, but are not limited to:

- U.S. government agencies – determination of direct versus indirect government support and whether any contingencies exist with respect to the timely payment of principal and interest.
- Foreign government – estimates of appropriate market spread versus underlying related sovereign treasury curve(s) dependent on liquidity and direct or contingent support.
- Municipals – overall credit quality, including assessments of the level and variability of: sources of payment such as income, sales or property taxes, levies or user fees; credit support such as insurance; state or local economic and political base; natural resource availability; and susceptibility to natural or man-made catastrophic events such as hurricanes, earthquakes or acts of terrorism.

Table of Contents

- Corporate fixed maturities – overall credit quality, including assessments of the level and variability of: economic sensitivity; liquidity; corporate financial policies; management quality; regulatory environment; competitive position; ownership; restrictive covenants; and security or collateral.
- Residential mortgage-backed securities – estimates of prepayment speeds based upon: historical prepayment rate trends; underlying collateral interest rates; geographic concentration; vintage year; borrower credit quality characteristics; interest rate and yield curve forecasts; government or monetary authority support programs; tax policies; delinquency/default trends; and, in the case of non-agency collateralized mortgage obligations, severity of loss upon default and length of time to recover proceeds following default.
- Commercial mortgage-backed securities – overall credit quality, including assessments of the value and supply/demand characteristics of: collateral type such as office, retail, residential, lodging, or other; geographic concentration by region, state, metropolitan statistical area and locale; vintage year; historical collateral performance including defeasance, delinquency, default and special servicer trends; and capital structure support features.
- Asset-backed securities – overall credit quality, including assessments of the underlying collateral type such as credit card receivables, auto loan receivables and equipment lease receivables; geographic diversification; vintage year; historical collateral performance including delinquency, default and casualty trends; economic conditions influencing use rates and resale values; and contract structural support features.

Generally, all prices provided by the pricing service, except actively traded securities with quoted market prices, are reported as Level 2.

The Company holds privately placed fixed maturity securities and certain other fixed maturity securities that do not have an active market and for which the pricing service cannot provide fair values. The Company determines fair values for these securities using either matrix pricing utilizing the market approach or broker quotes. The Company will use observable market data as inputs into the fair value applications, as discussed in the determination of Level 2 fair values, to the extent it is available, but is also required to use a certain amount of unobservable judgment due to the illiquid nature of the securities involved. Unobservable judgment reflected in the Company’s matrix model accounts for estimates of additional spread required by market participants for factors such as issue size, structural complexity, high bond coupon or other unique features. These matrix-priced securities are reported as Level 2 or Level 3, depending on the significance of the impact of unobservable judgment on the security’s value. Additionally, the Company may obtain non-binding broker quotes which are reported as Level 3.

Equity Securities

Level 1 consists of publicly traded securities, including exchange traded funds, valued at quoted market prices. Level 2 includes securities that are valued using pricing for similar securities and pricing models that incorporate observable inputs. Level 3 consists of common or preferred stock of private companies for which observable inputs are not available.

The Company utilizes a third party pricing service for the valuation of the majority of its equity securities and receives one quote for each equity security. When quoted market prices in an active market are available, they are provided by the pricing service as the fair value and such values are classified as Level 1. The Company holds certain equity securities that have been issued by privately-held entities that do not have an active market and for which the pricing service cannot provide fair values. Generally, the Company estimates fair value for these securities based on the issuer’s book value and market multiples. These securities are reported as Level 2 or Level 3 depending on the significance of the impact of unobservable judgment on the security’s value. Additionally, the company may obtain non-binding broker quotes which are reported as Level 3.

Other Investments

Other investments include mortgage participations and other mortgage loans, overseas trust funds required in connection with our Lloyd's business and cost basis limited partnerships. Fair values of mortgage participations and other mortgage loans are estimated by discounting the contractual cash flows using the rates at which similar loans would be made to borrowers with comparable credit ratings and are reported as Level 3. Fair values of overseas trust funds are provided by the investment manager based on quoted prices for similar instruments in active markets and are reported as Level 2. The fair values of cost basis limited partnerships are based on the net asset value provided by the general partner and recent financial information and are reported as Level 3.

Table of Contents

Debt

The fair value of debt is estimated based on quoted market prices. If a quoted market price is not available, fair values are estimated using discounted cash flows that are based on current interest rates and yield curves for debt issuances with maturities and credit risks consistent with the debt being valued. Debt is reported as Level 2.

The estimated fair value of the financial instruments were as follows:

| | June 30, 2015 | | December 31, 2014 | |
|---|---|---|---|---|
| (in millions) | Carrying Value | Fair Value | Carrying Value | Fair Value |
| Financial Assets | | | | |
| Cash and cash equivalents | $ 583.7 | $ 583.7 | $ 373.3 | $ 373.3 |
| Fixed maturities | 6,835.0 | 6,835.0 | 7,378.1 | 7,378.1 |
| Equity securities | 565.6 | 565.6 | 580.8 | 580.8 |
| Other investments | 285.9 | 290.1 | 267.4 | 272.2 |
| Total financial assets | $ 8,270.2 | $ 8,274.4 | $ 8,599.6 | $ 8,604.4 |
| Financial Liabilities | | | | |
| Debt | $ 835.1 | $ 961.2 | $ 903.5 | $ 1,021.7 |

The Company has processes designed to ensure that the values received from its third party pricing service are accurately recorded, that the data inputs and valuation techniques utilized are appropriate and consistently applied and that the assumptions are reasonable and consistent with the objective of determining fair value. The Company performs a review of the fair value hierarchy classifications and of prices received from its pricing service on a quarterly basis. The Company reviews the pricing services' policies describing its methodology, processes, practices and inputs, including various financial models used to value securities. Also, the Company reviews the portfolio pricing, including securities with changes in prices that exceed a defined threshold are verified to independent sources, if available. If upon review, the Company is not satisfied with the validity of a given price, a pricing challenge would be submitted to the pricing service along with supporting documentation for its review. The Company does not adjust quotes or prices obtained from the pricing service unless the pricing service agrees with the Company's challenge. During 2015 and 2014, the Company did not adjust any prices received from brokers or its pricing service.

Changes in the observability of valuation inputs may result in a reclassification of certain financial assets or liabilities within the fair value hierarchy. Reclassifications between levels of the fair value hierarchy are reported as of the beginning of the period in which the reclassification occurs. As previously discussed, the Company utilizes a third party pricing service for the valuation of the majority of its fixed maturities and equity securities. The pricing service has indicated that it will only produce an estimate of fair value if there is objectively verifiable information to produce a valuation. If the pricing service discontinues pricing an investment, the Company will use observable market data to the extent it is available, but may also be required to make assumptions for market based inputs that are unavailable due to market conditions.

The following tables provide, for each hierarchy level, the Company's assets that were measured at fair value on a recurring basis.

| | June 30, 2015 | | | |
|---|---|---|---|---|
| (in millions) | Total | Level 1 | Level 2 | Level 3 |
| Fixed maturities: | | | | |
| U.S. Treasury and government agencies | $ 442.2 | $ 163.0 | $ 279.2 | $ - |
| Foreign government | 204.3 | 22.8 | 181.5 | - |
| Municipal | 1,119.1 | - | 1,092.1 | 27.0 |
| Corporate | 3,657.0 | - | 3,647.6 | 9.4 |
| Residential mortgage-backed, U.S. agency backed | 681.2 | - | 681.2 | - |
| Residential mortgage-backed, non-agency | 85.4 | - | 85.4 | - |
| Commercial mortgage-backed | 537.0 | - | 519.0 | 18.0 |
| Asset-backed | 108.8 | - | 107.5 | 1.3 |
| Total fixed maturities | 6,835.0 | 185.8 | 6,593.5 | 55.7 |
| Equity securities | 556.0 | 554.7 | - | 1.3 |
| Other investments | 99.1 | - | 95.3 | 3.8 |
| Total investment assets at fair value | $ 7,490.1 | $ 740.5 | $ 6,688.8 | $ 60.8 |

Table of Contents

| | December 31, 2014 | | | |
|---|---|---|---|---|
| (in millions) | Total | Level 1 | Level 2 | Level 3 |
| Fixed maturities: | | | | |
| U.S. Treasury and government agencies | $ 520.4 | $ 233.5 | $ 286.9 | $ - |
| Foreign government | 354.0 | 43.3 | 310.7 | - |
| Municipal | 1,138.0 | - | 1,112.3 | 25.7 |
| Corporate | 3,880.8 | - | 3,871.2 | 9.6 |
| Residential mortgage-backed, U.S. agency backed | 689.2 | - | 689.2 | - |
| Residential mortgage-backed, non-agency | 99.9 | - | 99.9 | - |
| Commercial mortgage-backed | 527.8 | - | 506.4 | 21.4 |
| Asset-backed | 168.0 | - | 168.0 | - |
| Total fixed maturities | 7,378.1 | 276.8 | 7,044.6 | 56.7 |
| Equity securities | 571.5 | 570.3 | - | 1.2 |
| Other investments | 136.4 | - | 132.6 | 3.8 |
| Total investment assets at fair value | $ 8,086.0 | $ 847.1 | $ 7,177.2 | $ 61.7 |

The following tables provide, for each hierarchy level, the Company's estimated fair values of financial instruments that were not carried at fair value:

| | June 30, 2015 | | | |
|---|---|---|---|---|
| (in millions) | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Cash and cash equivalents | $ 583.7 | $ 583.7 | $ - | $ - |
| Equity securities | 9.6 | - | 9.6 | - |
| Other investments | 191.0 | - | - | 191.0 |
| Liabilities: | | | | |
| Debt | $ 961.2 | $ - | $ 961.2 | $ - |

| | December 31, 2014 | | | |
|---|---|---|---|---|
| (in millions) | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Cash and cash equivalents | $ 373.3 | $ 373.3 | $ - | $ - |
| Equity securities | 9.3 | - | 9.3 | - |
| Other investments | 135.8 | - | - | 135.8 |
| Liabilities: | | | | |
| Debt | $ 1,021.7 | $ - | $ 1,021.7 | $ - |

Table of Contents

The tables below provide a reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3).

| | Fixed Maturities | | | | | | |
|---|---|---|---|---|---|---|---|
| (in millions) | Municipal | Corporate | Commercial mortgage-backed | Asset-backed | Total | Equity and Other | Total Assets |
| Three Months Ended June 30, 2015 | | | | | | | |
| Balance April 1, 2015 | $ 27.2 | $ 9.5 | $ 20.9 | $ 0.8 | $ 58.4 | $ 5.1 | $ 63.5 |
| Transfers into Level 3 | - | - | - | 0.5 | 0.5 | - | 0.5 |
| Total gains (losses): | | | | | | | |
| Included in earnings | - | 0.1 | - | - | 0.1 | - | 0.1 |
| Included in other comprehensive income - net depreciation on available-for-sale securities | (1.2) | (0.1) | (0.9) | - | (2.2) | - | (2.2) |
| Purchases and sales: | | | | | | | |
| Purchases | 1.4 | - | - | - | 1.4 | - | 1.4 |
| Sales | (0.4) | (0.1) | (2.0) | - | (2.5) | - | (2.5) |
| Balance June 30, 2015 | $ 27.0 | $ 9.4 | $ 18.0 | $ 1.3 | $ 55.7 | $ 5.1 | $ 60.8 |
| Three Months Ended June 30, 2014 | | | | | | | |
| Balance April 1, 2014 | $ 29.6 | $ 13.2 | $ 22.5 | $ - | $ 65.3 | $ 4.8 | $ 70.1 |
| Transfers out of Level 3 | (2.6) | - | - | - | (2.6) | - | (2.6) |
| Total gains: | | | | | | | |
| Included in other comprehensive income - net appreciation on available-for-sale securities | 0.3 | - | 0.4 | - | 0.7 | - | 0.7 |
| Sales | (0.5) | - | (0.4) | - | (0.9) | - | (0.9) |
| Balance June 30, 2014 | $ 26.8 | $ 13.2 | $ 22.5 | $ - | $ 62.5 | $ 4.8 | $ 67.3 |

Table of Contents

| (in millions) | Fixed Maturities Municipal | Corporate | Residential mortgage-backed, non-agency | Commercial mortgage-backed | Asset-backed | Total | Equity and Other | Total Assets |
|---|---|---|---|---|---|---|---|---|
| Six Months Ended June 30, 2015 | | | | | | | | |
| Balance January 1, 2015 | $ 25.7 | $ 9.6 | $ - | $ 21.4 | $ - | $ 56.7 | $ 5.0 | $ 61.7 |
| Transfers into Level 3 | - | - | - | - | 1.3 | 1.3 | - | 1.3 |
| Total gains (losses): | | | | | | | | |
| Included in earnings | - | 0.1 | - | - | - | 0.1 | - | 0.1 |
| Included in other comprehensive income-net (depreciation) appreciation on available-for-sale securities | (0.8) | (0.2) | - | (0.6) | - | (1.6) | 0.1 | (1.5) |
| Purchases and sales: | | | | | | | | |
| Purchases | 3.1 | - | - | - | - | 3.1 | - | 3.1 |
| Sales | (1.0) | (0.1) | - | (2.8) | - | (3.9) | - | (3.9) |
| Balance June 30, 2015 | $ 27.0 | $ 9.4 | $ - | $ 18.0 | $ 1.3 | $ 55.7 | $ 5.1 | $ 60.8 |
| | | | | | | | | |
| Six Months Ended June 30, 2014 | | | | | | | | |
| Balance January 1, 2014 | $ 25.6 | $ 13.0 | $ 0.5 | $ 22.9 | $ - | $ 62.0 | $ 42.2 | $ 104.2 |
| Transfers into Level 3 | 2.2 | - | - | - | - | 2.2 | - | 2.2 |
| Transfers out of Level 3 | (2.6) | - | - | - | - | (2.6) | (37.4) | (40.0) |
| Total gains (losses): | | | | | | | | |
| Included in other comprehensive income-net appreciation on available-for-sale securities | 0.6 | 0.2 | - | 0.7 | - | 1.5 | - | 1.5 |
| Purchases and sales: | | | | | | | | |
| Purchases | 2.5 | - | - | - | - | 2.5 | - | 2.5 |
| Sales | (1.5) | - | (0.5) | (1.1) | - | (3.1) | - | (3.1) |
| Balance June 30, 2014 | $ 26.8 | $ 13.2 | $ - | $ 22.5 | $ - | $ 62.5 | $ 4.8 | $ 67.3 |

During the three and six months ended June 30, 2015 and 2014, the Company transferred fixed maturities between Level 2 and Level 3 primarily as a result of assessing the significance of unobservable inputs on the fair value measurement. There were no transfers between Level 1 and Level 2 during the three months or six months ended June 30, 2015 or 2014.

Table of Contents

There were no Level 3 liabilities held by the Company for the six months ended June 30, 2015 and 2014. The following table summarizes changes in fair value that were recorded in net income for Level 3 assets:

| (in millions) | Three Months Ended June 30, 2015 | 2014 | Six Months Ended June 30, 2015 | 2014 |
|---|---|---|---|---|
| | Net Investment Income | | Net Investment Income | |
| Level 3 Assets: | | | | |
| Fixed maturities: | | | | |
| Corporates | $ 0.1 | $ - | $ 0.1 | $ - |

The following table provides quantitative information about the significant unobservable inputs used by the Company in the fair value measurements of Level 3 assets. Where discounted cash flows were used in the valuation of fixed maturities, the internally-developed discount rate was adjusted by the significant unobservable inputs shown in the table. Valuations for securities based on broker quotes for which there was a lack of transparency as to inputs used to develop the valuations have been excluded.

| | | | June 30, 2015 | | December 31, 2014 | |
|---|---|---|---|---|---|---|
| (in millions) | Valuation Technique | Significant Unobservable Inputs | Fair Value | Range (Wtd Average) | Fair Value | Range (Wtd Average) |
| Fixed maturities: | | | | | | |
| Municipal | Discounted cash flow | Discount for: | $ 27.0 | | $ 25.7 | |
| | | Small issue size | | 0.6-6.8% (2.5%) | | 0.6-4.5% (2.0%) |
| | | Credit stress | | 0.9-1.5% (1.2%) | | N/A |
| | | Above-market coupon | | 0.3-1.0% (0.4%) | | 0.3-1.0% (0.4%) |
| Corporate | Discounted cash flow | Discount for: | 9.1 | | 9.4 | |
| | | Small issue size | | 0.5-1.0% (0.8%) | | 0.5-1.0% (0.7%) |
| | | Above-market coupon | | 0.3-0.8% (0.6%) | | 0.3-0.8% (0.6%) |
| Commercial mortgage-backed | Discounted cash flow | Discount for: | 18.0 | | 21.4 | |

| | | | | | | |
|---|---|---|---|---|---|---|
| | | Small issue size | | 0.5-1.0% (0.5%) | | 0.5% (0.5%) |
| | | Above-market coupon | | 0.5% (0.5%) | | 0.5-0.8% (0.5%) |
| | | Lease structure | | 0.3% (0.3%) | | 0.3% (0.3%) |
| | | Credit stress | | N/A | | 0.5% (0.5%) |
| Asset-backed | Discounted cash flow | Discount for: | 1.3 | | - | |
| | | Small issue size | | 0.7-0.8% (0.7%) | | N/A |
| Equity securities | Market comparables | Net tangible asset market multiples | 1.1 | 1.0X (1.0X) | 1.1 | 1.0X (1.0X) |
| Other | Discounted cash flow | Discount rate | 3.8 | 18.0% (18.0%) | 3.8 | 18.0% (18.0%) |

Significant increases (decreases) in any of the above inputs in isolation would result in a significantly lower (higher) fair value measurement. There were no interrelationships between these inputs which might magnify or mitigate the effect of changes in unobservable inputs on the fair value measurement.

Table of Contents

8. Pension and Other Postretirement Benefit Plans

The components of net periodic pension cost for defined benefit pension and other postretirement benefit plans included in the Company's results of operations are as follows:

| | Three Months Ended June 30, | | | |
|---|---|---|---|---|
| | 2015 | 2014 | 2015 | 2014 |
| (in millions) | Pension Plans | | Postretirement Plans | |
| Service cost - benefits earned during the period | $ 0.4 | $ 0.3 | $ - | $ - |
| Interest cost | 7.3 | 8.5 | 0.1 | 0.2 |
| Expected return on plan assets | (7.9) | (9.1) | - | - |
| Recognized net actuarial loss | 4.8 | 2.9 | 0.1 | - |
| Amortization of prior service cost | - | 0.1 | (0.3) | (0.5) |
| Curtailment gain | (1.8) | - | - | - |
| Net periodic pension cost (benefit) | $ 2.8 | $ 2.7 | $ (0.1) | $ (0.3) |

| | Six Months Ended June 30, | | | |
|---|---|---|---|---|
| | 2015 | 2014 | 2015 | 2014 |
| (in millions) | Pension Plans | | Postretirement Plans | |
| Service cost - benefits earned during the period | $ 0.7 | $ 0.7 | $ - | $ - |
| Interest cost | 14.6 | 16.9 | 0.3 | 0.4 |
| Expected return on plan assets | (15.7) | (18.3) | - | - |
| Recognized net actuarial loss | 7.8 | 5.8 | 0.1 | - |
| Amortization of prior service cost | - | 0.1 | (0.7) | (0.9) |
| Curtailment gain | (1.8) | - | - | - |
| Net periodic pension cost (benefit) | $ 5.6 | $ 5.2 | $ (0.3) | $ (0.5) |

In the second quarter of 2015, the Company recognized a $1.8 million benefit due to the disposal of the U.K. motor business. Included in the table above in recognized net actuarial loss was an equal and offsetting expense.

Table of Contents

9. Other Comprehensive Income

The following table provides changes in other comprehensive income.

| | Three Months Ended June 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2015 | | | 2014 | | |
| (in millions) | Pre-Tax | Tax Benefit (Expense) | Net of Tax | Pre-Tax | Tax Benefit (Expense) | Net of Tax |
| Unrealized gains (losses) on available-for-sale securities and derivative instruments: | | | | | | |
| Unrealized (losses) gains arising during period (net of pre-tax, ceded unrealized gains of $0.7 million for the three months ended June 30, 2014) | $ (128.2) | $ 44.8 | $ (83.4) | $ 83.2 | $ (29.2) | $ 54.0 |
| Less: | | | | | | |
| Amount of realized gains from sales and other | (14.4) | 1.9 | (12.5) | (22.4) | 2.6 | (19.8) |
| Portion of other-than-temporary impairment losses recognized in earnings | 1.9 | (0.7) | 1.2 | 0.1 | - | 0.1 |
| Net unrealized (losses) gains | (140.7) | 46.0 | (94.7) | 60.9 | (26.6) | 34.3 |
| Pension and postretirement benefits: | | | | | | |
| Net actuarial losses and prior service costs arising in the period | (4.2) | 0.9 | (3.3) | - | - | - |
| Amortization of net actuarial loss and prior service cost recognized as net periodic benefit cost | 4.7 | (1.3) | 3.4 | 2.5 | (0.9) | 1.6 |
| Net pension and postretirement benefits | 0.5 | (0.4) | 0.1 | 2.5 | (0.9) | 1.6 |
| Cumulative foreign currency translation adjustment: | | | | | | |
| Foreign currency translation recognized during the period | 11.9 | (4.2) | 7.7 | 4.8 | (1.7) | 3.1 |
| Other comprehensive (loss) income | $ (128.3) | $ 41.4 | $ (86.9) | $ 68.2 | $ (29.2) | $ 39.0 |

| Six Months Ended June 30, | | | | | |
|---|---|---|---|---|---|
| 2015 | | | 2014 | | |
| | Tax Benefit | Net of | | Tax | |