

AETNA INC /PA/
Form 10-Q
October 28, 2014

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 September 30, 2014
or

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

For the transition period from _____ to _____

Commission File Number: 1-16095

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

Pennsylvania
(State or other jurisdiction of incorporation or organization)
151 Farmington Avenue, Hartford, CT
(Address of principal executive offices)
Registrant's telephone number, including area code:

23-2229683
(I.R.S. Employer Identification No.)
06156
(Zip Code)
(860) 273-0123

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. 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

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company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer

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

Accelerated filer

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

There were 351.7 million shares of the registrant’s voting common stock with a par value of \$.01 per share outstanding at September 30, 2014.

Aetna Inc.
Form 10-Q
For the Quarterly Period Ended September 30, 2014

Unless the context otherwise requires, references to the terms “we”, “our” or “us” used throughout this Quarterly Report on Form 10-Q (except the Report of Independent Registered Public Accounting Firm on page 37), refer to Aetna Inc. (a Pennsylvania corporation) (“Aetna”) and its subsidiaries (collectively, the “Company”).

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Part I. Financial Information

Item 1. Financial Statements

Consolidated Statements of Income
(Unaudited)

(Millions, except per common share data)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenue:				
Health care premiums	\$12,588.4	\$11,025.2	\$36,916.2	\$28,512.3
Other premiums	538.8	525.9	1,652.1	1,561.5
Group annuity contract conversion premium	—	54.1	—	54.1
Fees and other revenue ⁽¹⁾	1,337.7	1,233.1	3,876.0	3,326.1
Net investment income	234.6	210.0	707.1	670.1
Net realized capital gains (losses)	28.3	(12.7)	80.6	(12.2)
Total revenue	14,727.8	13,035.6	43,232.0	34,111.9
Benefits and expenses:				
Health care costs ⁽²⁾	10,354.5	9,161.9	30,245.6	23,548.3
Current and future benefits	521.6	557.0	1,625.9	1,655.4
Benefit expense on group annuity contract conversion	—	54.1	—	54.1
Operating expenses:				
Selling expenses	422.3	353.9	1,238.1	983.3
General and administrative expenses	2,292.4	1,950.6	6,528.2	5,154.8
Total operating expenses	2,714.7	2,304.5	7,766.3	6,138.1
Interest expense	80.6	86.1	247.5	247.4
Amortization of other acquired intangible assets	59.5	65.3	183.6	149.5
Loss on early extinguishment of long-term debt	—	—	91.9	—
Reduction of reserve for anticipated future losses on discontinued products	—	—	—	(86.0)
Total benefits and expenses	13,730.9	12,228.9	40,160.8	31,706.8
Income before income taxes	996.9	806.7	3,071.2	2,405.1
Income taxes:				
Current	430.4	283.5	1,199.4	826.0
Deferred	(32.3)	4.2	56.4	36.0
Total income taxes	398.1	287.7	1,255.8	862.0
Net income including non-controlling interests	598.8	519.0	1,815.4	1,543.1
Less: Net income (loss) attributable to non-controlling interests	4.3	.4	6.6	(1.6)
Net income attributable to Aetna	\$594.5	\$518.6	\$1,808.8	\$1,544.7
Earnings per common share:				
Basic	\$1.68	\$1.40	\$5.06	\$4.39
Diluted	\$1.67	\$1.38	\$5.01	\$4.35

⁽¹⁾ Fees and other revenue include administrative services contract member co-payments and plan sponsor reimbursements related to our mail order and specialty pharmacy operations of \$26.4 million and \$74.6 million (net of pharmaceutical and processing costs of \$323.4 million and \$914.3 million) for the three and nine months ended September 30, 2014, respectively, and \$21.7 million and \$62.3 million (net of pharmaceutical and processing costs of \$286.3 million and \$834.0 million) for the three and nine months ended September 30, 2013,

respectively.

(2) Health care costs have been reduced by Insured member co-payments related to our mail order and specialty pharmacy operations of \$25.9 million and \$83.8 million for the three and nine months ended September 30, 2014, respectively, and \$25.9 million and \$85.0 million for the three and nine months ended September 30, 2013, respectively.

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

Page 1

Consolidated Statements of Comprehensive Income
(Unaudited)

(Millions)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income including non-controlling interests	\$598.8	\$519.0	\$1,815.4	\$1,543.1
Other comprehensive income (loss), net of tax:				
Previously impaired debt securities: ⁽¹⁾				
Net unrealized losses				
\$(6.9), \$(9.7), \$(1.8) and \$(62.8) pretax	(4.5	) (6.3	) (1.2	) (40.8
Less: reclassification of (losses) gains to earnings				
\$(2.8), \$(3.1), \$.3 and \$(31.7) pretax	(1.8	) (2.0	) .2	) (20.6
Total previously impaired debt securities ⁽¹⁾	(2.7	) (4.3	) (1.4	) (20.2
All other securities:				
Net unrealized (losses) gains				
\$(97.7), \$(12.0), \$326.9 and \$(740.1) pretax	(63.5	) (7.8	) 212.5	) (481.1
Less: reclassification of gains (losses) to earnings				
\$(7.6), \$(21.6), \$9.5 and \$(26.4) pretax	5.0	) (14.1	) 6.2	) (17.2
Total all other securities	(68.5	) 6.3	206.3	) (463.9
Foreign currency and derivatives:				
Net unrealized (losses) gains				
\$(16.9), \$6.1, \$(55.4) and \$35.2 pretax	(11.0	) 4.0	) (36.0	) 22.9
Less: reclassification of (losses) gains to earnings				
\$(1.4), \$(1.4), \$12.8 and \$(4.0) pretax	(.9	) (.9	) 8.3	) (2.6
Total foreign currency and derivatives	(10.1	) 4.9	) (44.3	) 25.5
Pension and other postretirement benefit (“OPEB”) plans:				
Amortization of net actuarial losses				
\$(11.9), \$(19.6), \$(35.7) and \$(58.3) pretax	7.8	12.7	23.2	37.9
Amortization of prior service credit				
\$(1.1), \$1.1, \$3.1 and \$3.0 pretax	(.7	) (.7	) (2.0	) (2.0
Total pension and OPEB plans	7.1	12.0	21.2	35.9
Other comprehensive (loss) income	(74.2	) 18.9	181.8	) (422.7
Comprehensive income including non-controlling interests	524.6	537.9	1,997.2	1,120.4
Less: Comprehensive income (loss) attributable to non-controlling interests	4.3	.4	6.6	) (1.6
Comprehensive income attributable to Aetna	\$520.3	\$537.5	\$1,990.6	\$1,122.0

⁽¹⁾ Represents unrealized (losses) gains on the non-credit related component of impaired debt securities that we do not intend to sell and subsequent changes in the fair value of any previously impaired security.

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

Consolidated Balance Sheets

(Millions)	(Unaudited)	
	At September 30, 2014	At December 31, 2013
Assets:		
Current assets:		
Cash and cash equivalents	\$1,707.1	\$1,412.3
Investments	2,462.0	2,063.8
Premiums receivable, net	1,414.2	1,331.2
Other receivables, net	1,987.4	1,780.8
Accrued investment income	217.7	211.1
Collateral received under securities loan agreements	870.3	792.6
Income taxes receivable	29.4	69.2
Deferred income taxes	501.5	521.5
Other current assets	2,275.3	1,536.4
Total current assets	11,464.9	9,718.9
Long-term investments	21,871.5	20,935.0
Reinsurance recoverables	757.2	782.7
Goodwill	10,295.2	10,227.5
Other acquired intangible assets, net	1,934.1	2,094.1
Property and equipment, net	668.9	721.9
Other long-term assets	1,632.0	1,419.2
Separate Accounts assets	4,401.8	3,972.5
Total assets	\$53,025.6	\$49,871.8
Liabilities and shareholders' equity:		
Current liabilities:		
Health care costs payable	\$5,592.8	\$4,547.4
Future policy benefits	713.7	734.4
Unpaid claims	715.0	705.4
Unearned premiums	554.9	458.7
Policyholders' funds	1,955.7	1,727.3
Collateral payable under securities loan agreements	870.3	792.6
Short-term debt	75.0	—
Current portion of long-term debt	232.1	387.3
Accrued expenses and other current liabilities	3,923.1	3,226.9
Total current liabilities	14,632.6	12,580.0
Future policy benefits	6,490.9	6,656.8
Unpaid claims	1,654.1	1,619.3
Policyholders' funds	1,194.3	1,188.0
Long-term debt, less current portion	7,606.3	7,865.3
Deferred income taxes	1,033.3	864.2
Other long-term liabilities	1,029.9	1,047.5
Separate Accounts liabilities	4,401.8	3,972.5
Total liabilities	38,043.2	35,793.6
Commitments and contingencies (Note 13)		
Shareholders' equity:		
Common stock (\$.01 par value; 2.6 billion shares authorized and 351.7 million shares issued		

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and outstanding in 2014; 2.6 billion shares authorized and 362.2 million shares issued and

outstanding in 2013) and additional paid-in capital	4,501.4	4,382.2
Retained earnings	11,150.1	10,555.4
Accumulated other comprehensive loss	(730.3	) (912.1
Total Aetna shareholders' equity	14,921.2	14,025.5
Non-controlling interests	61.2	52.7
Total equity	14,982.4	14,078.2
Total liabilities and equity	\$53,025.6	\$49,871.8

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

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Consolidated Statements of Shareholders' Equity
(Unaudited)

(Millions)	Number of Common Shares Outstanding	Attributable to Aetna Common			Accumulated Other Comprehensive Loss	Total Aetna Shareholders' Equity	Non-Controlling Interests	Total Equity
		Stock and Additional Paid-in Capital	Retained Earnings					
Nine Months Ended September 30, 2014								
Balance at December 31, 2013	362.2	\$4,382.2	\$10,555.4	\$ (912.1)	\$14,025.5	\$ 52.7	\$14,078.2	
Net income	—	—	1,808.8	—	1,808.8	6.6	1,815.4	
Other increases in non- controlling interest	—	—	—	—	—	1.9	1.9	
Other comprehensive income (Note 7)	—	—	—	181.8	181.8	—	181.8	
Common shares issued for benefit plans, including tax benefits	2.5	119.3	—	—	119.3	—	119.3	
Repurchases of common shares	(13.0)	(.1)	(974.9)	—	(975.0)	—	(975.0)	
Dividends declared	—	—	(239.2)	—	(239.2)	—	(239.2)	
Balance at September 30, 2014	351.7	\$4,501.4	\$11,150.1	\$ (730.3)	\$14,921.2	\$ 61.2	\$14,982.4	
Nine Months Ended September 30, 2013								
Balance at December 31, 2012	327.6	\$1,095.3	\$10,343.9	\$ (1,033.4)	\$10,405.8	\$ 23.4	\$10,429.2	
Net income (loss)	—	—	1,544.7	—	1,544.7	(1.6)	1,543.1	
Other increases in non- controlling interest	—	—	—	—	—	29.5	29.5	
Other comprehensive loss (Note 7)	—	—	—	(422.7)	(422.7)	—	(422.7)	
Common shares issued to acquire Coventry	52.2	3,064.6	—	—	3,064.6	—	3,064.6	
Common shares issued for benefit plans, including tax benefits	3.9	196.7	—	—	196.7	—	196.7	
Repurchases of common shares	(16.2)	(.2)	(957.5)	—	(957.7)	—	(957.7)	
Dividends declared	—	—	(213.2)	—	(213.2)	—	(213.2)	
	367.5	\$4,356.4	\$10,717.9	\$ (1,456.1)	\$13,618.2	\$ 51.3	\$13,669.5	

Balance at September
30, 2013

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

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Consolidated Statements of Cash Flows
(Unaudited)

(Millions)	Nine Months Ended September 30,	
	2014	2013
Cash flows from operating activities:		
Net income including non-controlling interests	\$1,815.4	\$1,543.1
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized capital (gains) losses	(80.6	) 12.2
Depreciation and amortization	467.7	406.5
Debt fair value amortization	(42.9	) (24.2
Equity in earnings of affiliates, net	(31.8	) (18.2
Stock-based compensation expense	124.2	90.6
Reduction of reserve for anticipated future losses on discontinued products	—	(86.0
Reversal of allowance and gain on sale of reinsurance recoverable	—	(49.4
Amortization of net investment premium	54.3	38.1
Loss on early extinguishment of long-term debt	91.9	—
Changes in assets and liabilities:		
Accrued investment income	(6.6	) 9.4
Premiums due and other receivables	(395.7	) (308.5
Income taxes	107.9	99.4
Other assets and other liabilities	194.0	(38.1
Health care and insurance liabilities	784.0	(16.9
Other, net	(3.1	) (3.4
Net cash provided by operating activities	3,078.7	1,654.6
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	6,360.3	11,037.9
Cost of investments	(7,150.8	) (10,219.1
Additions to property, equipment and software	(261.1	) (331.6
Cash used for acquisitions, net of cash acquired	(70.7	) (1,635.9
Other, net	10.0	2.5
Net cash used for investing activities	(1,112.3	) (1,146.2
Cash flows from financing activities:		
Repayment of long-term debt	(1,214.8) —
Issuance of long-term debt	741.9	—
Net issuance of short-term debt	75.0	—
Deposits and interest credited for investment contracts	3.4	3.4
Withdrawals of investment contracts	(2.1	) (9.7
Common shares issued under benefit plans, net	(36.0	) 39.0
Stock-based compensation tax benefits	25.7	62.9
Common shares repurchased	(975.0	) (957.7
Dividends paid to shareholders	(241.6	) (205.2
Collateral on interest rate swaps	(49.9	) 32.6
Contributions, non-controlling interests	1.8	29.5
Net cash used for financing activities	(1,671.6	) (1,005.2
Net increase (decrease) in cash and cash equivalents	294.8	(496.8
Cash and cash equivalents, beginning of period	1,412.3	2,579.2
Cash and cash equivalents, end of period	\$1,707.1	\$2,082.4
Supplemental cash flow information:		

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Interest paid	\$260.2	\$229.6
Income taxes paid	1,122.2	699.5

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

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Condensed Notes to Consolidated Financial Statements
(Unaudited)

1. Organization

We conduct our operations in three business segments:

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

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

Large Case Pensions manages a variety of retirement products (including pension and annuity products) primarily for tax-qualified pension plans. These products provide a variety of funding and benefit payment distribution options and other services. Large Case Pensions also includes certain discontinued products (refer to Note 16 beginning on page 35 for additional information).

On May 7, 2013 (the “Acquisition Date”), we completed the acquisition of Coventry Health Care, Inc. (“Coventry”) in a transaction valued at approximately \$8.7 billion, including the fair value of Coventry’s outstanding debt. Refer to Note 3 beginning on page 9 for additional information.

2. Summary of Significant Accounting Policies

Interim Financial Statements

These interim financial statements necessarily rely on estimates, including assumptions as to annualized tax rates. In the opinion of management, all adjustments necessary for a fair statement of results for the interim periods have been made. All such adjustments are of a normal, recurring nature. The accompanying unaudited consolidated financial statements and related notes should be read in conjunction with the consolidated financial statements and related notes presented in our 2013 Annual Report on Form 10-K (our “2013 Annual Report”). Certain financial information that is normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles (“GAAP”), but that is not required for interim reporting purposes, has been condensed or omitted. We have

omitted certain footnote disclosures that would

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substantially duplicate the disclosures in our 2013 Annual Report, unless the information contained in those disclosures materially changed and is required by GAAP. We evaluated subsequent events that occurred after September 30, 2014 through the date the financial statements were issued and determined there were no other items to disclose other than as disclosed in Note 11 beginning on page 28.

Reclassifications

Certain reclassifications were made to 2013 financial information to conform with the 2014 presentation.

Principles of Consolidation

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

Accounting for certain provisions of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, "Health Care Reform" or "ACA")

We are participating in certain public health insurance exchanges established pursuant to Health Care Reform. Under regulations established by the U.S. Department of Health and Human Services ("HHS"), HHS pays us a portion of the premium ("Premium Subsidy") and/or a portion of the health care costs ("Cost Sharing Subsidy") for low-income individual members. In addition, HHS administers certain risk management programs as described below.

We recognize monthly premiums received from members and the Premium Subsidy as premium revenue ratably over the contract period. The Cost Sharing Subsidy offsets health care costs when incurred. We record a liability if the Cost Sharing Subsidy is paid in advance or a receivable if incurred health care costs exceed the Cost Sharing Subsidy received to date.

Accounting for Health Care Reform's Reinsurance, Risk Adjustment and Risk Corridor (the "3Rs")

Reinsurance

Health Care Reform established a temporary three-year reinsurance program, whereby all issuers of major medical commercial insurance products and self-insured plan sponsors are required to contribute funding in amounts set by HHS. Funds collected will be utilized to reimburse issuers' high claims costs incurred for qualified individual members. The expense related to this required funding is reflected in general and administrative expenses for all of our insurance products with the exception of products associated with qualified individual members; this expense for qualified individual members is reflected as a reduction of premium revenue. When annual claim costs incurred by our qualified individual members exceed a specified attachment point, we are entitled to certain reimbursements from this program. We record a receivable and offset health care costs to reflect our estimate of these recoveries. As of September 30, 2014, we recorded a receivable under the temporary three-year reinsurance program of approximately \$162 million.

Risk Adjustment

Health Care Reform established a permanent risk adjustment program to transfer funds from qualified individual and small group insurance plans with below average risk scores to those respective plans with above average risk scores. Based on the risk of our qualified plan members relative to the average risk of members of other qualified plans in comparable markets, we estimate our ultimate 2014 risk adjustment receivable or payable and reflect the pro-rata year-to-date impact as an adjustment to our premium revenue.

Risk Corridor

Health Care Reform established a temporary three-year risk sharing program for qualified individual and small group insurance plans. Under this program we make (or receive) a payment to (or from) HHS based on the ratio of allowable costs to target costs (as defined by Health Care Reform). We record a risk corridor receivable or payable as an

adjustment to premium revenue on a pro-rata year-to-date basis based on our estimate of the ultimate 2014 risk sharing amount.

Collectively, as of September 30, 2014, we recorded an aggregate net payable of approximately \$97 million under the risk adjustment and risk corridor programs.

We will perform a final reconciliation and settlement with HHS of the 2014 Cost Sharing Subsidy and 3Rs during 2015.

New Accounting Standards

Fees Paid to the Federal Government by Health Insurers

Effective January 1, 2014, we adopted new accounting guidance relating to the recognition and income statement reporting of the mandated fee to be paid to the federal government by health insurers. This guidance applies to the new health insurer fee (“HIF”) included in Health Care Reform. This new accounting guidance resulted in the establishment on January 1, 2014, of a liability for our portion of the entire estimated 2014 annual HIF. This amount is reflected in accrued expenses and other liabilities with a corresponding amount reflected in other current assets. The estimated annual HIF is amortized into general and administrative expenses on a straight-line basis with a corresponding reduction in other current assets. The HIF for 2014 was paid in September 2014 and is not tax deductible.

Amendments to the Scope, Measurement and Disclosure Requirements of Investment Companies

Effective January 1, 2014, we adopted new accounting guidance relating to the approach for determining whether an entity is considered an investment company for accounting purposes. This guidance clarified the characteristics and set measurement and disclosure requirements for an investment company for accounting purposes. The adoption of this new guidance did not have an impact on our financial position or operating results.

Future Application of Accounting Standards

Accounting for Investments in Qualified Affordable Housing Projects

Effective January 1, 2015, we will be permitted to make an accounting policy election to adopt new accounting guidance relating to the recognition of amortization of investments in qualified affordable housing projects. The guidance sets forth a new method of measurement, referred to as the proportional amortization method, under which income and expense items related to qualified affordable housing projects would be recorded in the income taxes line item. If we elect to adopt this new guidance, it is not expected to have a material impact on our financial position or operating results.

Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity

Effective January 1, 2015, we will adopt amended accounting guidance related to when an entity reports a discontinued operation in its financial position and operating results. The guidance clarifies that a discontinued operation is required to be reported if the disposal represents a significant shift that has (or will have) a major effect on an entity’s operations and financial results when a component of an entity or a group of components of an entity are either classified as held for sale or are disposed of by sale. The amendments also require additional disclosures about discontinued operations. If we have a discontinued operation after the effective date, these changes could result in increased reporting and disclosure requirements in our financial statements.

Revenue from Contracts with Customers

Effective January 1, 2017, we will adopt new accounting guidance related to revenue recognition from contracts with customers. This new guidance removes most industry-specific revenue recognition requirements (insurance contracts are not covered by this guidance) and requires that an entity recognize revenue for the transfer of goods or services to a customer at an amount that reflects the consideration to which an entity expects to be entitled in exchange for the goods or services. The new guidance also requires additional disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts. The new guidance allows an entity to adopt the standard either through a full retrospective approach or a modified retrospective approach with a cumulative effect

adjustment to retained earnings. We are still assessing the impact of this standard on our financial position and operating results in addition to evaluating the transition method we will use when we adopt this standard.

Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures

Effective January 1, 2015, we will adopt new accounting guidance related to the accounting for repurchase-to-maturity transactions and repurchase financing arrangements. This guidance aligns the accounting for repurchase-to-maturity transactions and repurchase agreements executed as repurchase financings with other typical repurchase agreements, resulting in these transactions generally being accounted for as secured borrowings. The guidance also requires additional disclosures about repurchase agreements and other similar transactions. The adoption of this new guidance is not expected to have a material impact on our financial position or operating results.

Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period

Effective January 1, 2016, we will adopt new accounting guidance related to the accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period. This guidance clarifies that awards with these provisions should be treated as performance conditions that affect vesting, and do not impact the award's estimated grant-date fair value. Early adoption for this new guidance is permitted. The adoption of this new guidance will not have an impact on our financial position or operating results.

Disclosure of Uncertainties About an Entity's Ability to Continue as a Going Concern

Effective December 31, 2016, we will adopt amended accounting guidance related to management's evaluation about whether there is substantial doubt about an entity's ability to continue as a going concern and the related disclosures. The adoption of this new guidance is not expected to have a material impact on our financial position or operating results.

3. Acquisitions; Completed Disposition

Acquisition of the InterGlobal Group

In April 2014, we acquired the InterGlobal group ("InterGlobal"), a company that specializes in international private medical insurance for groups and individuals in the Middle East, Asia, Africa and Europe. The purchase price was not material, and the goodwill related to this acquisition was assigned to our Health Care segment.

Acquisition of Coventry

On the Acquisition Date, we acquired Coventry in a transaction (the "Merger") valued at approximately \$8.7 billion, including the \$1.8 billion fair value of Coventry's outstanding long-term debt.

Pro Forma Impact of the Acquisition of Coventry

The following table presents supplemental pro forma information for the nine months ended September 30, 2013, as if the Merger had occurred on January 1, 2012. The unaudited pro forma consolidated results are not necessarily indicative of what our consolidated results would have been had the Merger been completed on January 1, 2012. In addition, the unaudited pro forma consolidated results do not purport to project the future results of the combined company nor do they reflect the expected realization of any cost savings associated with the Merger.

(Millions, except per common share data)	Nine Months Ended September 30, 2013
Total revenue	\$38,906.6
Net income attributable to Aetna	1,775.3
Earnings per share:	
Basic	\$4.73
Diluted	4.68

The unaudited pro forma consolidated results for the nine months ended September 30, 2013 reflect the following pro forma adjustments:

- Elimination of intercompany transactions between Aetna and Coventry, primarily related to network rental fees.
- Foregone interest income associated with cash and cash equivalents and investments assumed to have been used to partially fund the Merger.
- Foregone interest income associated with adjusting the amortized cost of Coventry's investment portfolio to fair value as of the completion of the Merger.
- Elimination of historical Coventry intangible asset amortization expense and capitalized internal-use software amortization expense and addition of intangible asset amortization expense relating to intangibles valued as part of the acquisition.
- Interest expense was reduced for the amortization of the fair value adjustment to long-term debt.
- Elimination of transaction-related costs incurred by Aetna and Coventry during 2013.
- Adjustment of the above pro forma adjustments for the applicable tax impact.
- Conforming adjustments to align Coventry's presentation to Aetna's accounting policies.
- Elimination of revenue and directly identifiable costs related to the sale of Aetna's Missouri Medicaid business, Missouri Care, Incorporated ("Missouri Care"), to WellCare Health Plans, Inc. on March 31, 2013.

Completed Disposition

In connection with the acquisition of Coventry, on March 31, 2013, we completed the sale of Missouri Care to WellCare Health Plans, Inc. The sale price was not material, and the transaction did not have a material impact on our financial position or operating results.

4. Earnings Per Common Share

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

The computations of basic and diluted EPS for the three and nine months ended September 30, 2014 and 2013 are as follows:

(Millions, except per common share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income attributable to Aetna	\$594.5	\$518.6	\$1,808.8	\$1,544.7
Weighted average shares used to compute basic EPS	353.2	371.1	357.2	351.8
Dilutive effect of outstanding stock-based compensation awards	3.6	4.1	3.5	3.7
Weighted average shares used to compute diluted EPS	356.8	375.2	360.7	355.5
Basic EPS	\$1.68	\$1.40	\$5.06	\$4.39
Diluted EPS	\$1.67	\$1.38	\$5.01	\$4.35

The stock-based compensation awards excluded from the calculation of diluted EPS for the three and nine months ended September 30, 2014 and 2013 are as follows:

(Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Stock appreciation rights ("SARs" ⁽¹⁾)	—	—	.4	2.2
Market stock units ("MSUs" ⁽²⁾)	—	.4	.1	.4
Performance stock units ("PSUs" ⁽²⁾)	.8	.9	.8	.8
Performance stock appreciation rights ("PSARs" ⁽²⁾)	.7	.7	.4	.2

- (1) SARs are excluded from the calculation of diluted EPS if the exercise price is greater than the average market price of Aetna common shares during the period (i.e., the awards are anti-dilutive).
- (2) PSUs, certain MSUs with performance conditions and PSARs are excluded from the calculation of diluted EPS if all necessary performance conditions have not been satisfied at the end of the reporting period.

All outstanding stock options were included in the calculation of diluted EPS for the three and nine months ended September 30, 2014 and 2013.

In connection with the May 7, 2013 acquisition of Coventry, we issued approximately 52.2 million Aetna common shares in exchange for all the outstanding shares of Coventry common stock. Those Aetna common shares were outstanding, net of any subsequent share repurchases, and included in the calculation of weighted average shares used to compute basic EPS for the entire three and nine months ended September 30, 2014, as well as for the entire three months ended September 30, 2013, and from the Acquisition Date through September 30, 2013 for the nine months ended September 30, 2013, and weighted accordingly.

5. Operating Expenses

For the three and nine months ended September 30, 2014 and 2013, selling expenses (which include broker commissions, the variable component of our internal sales force compensation and premium taxes) and general and administrative expenses were as follows:

(Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Selling expenses	\$422.3	\$353.9	\$1,238.1	\$983.3
General and administrative expenses:				
Salaries and related benefits	1,134.4	1,119.4	3,354.0	2,914.5
Other general and administrative expenses ^{(1) (2) (3)}	1,158.0	831.2	3,174.2	2,240.3
Total general and administrative expenses ⁽⁴⁾	2,292.4	1,950.6	6,528.2	5,154.8
Total operating expenses	\$2,714.7	\$2,304.5	\$7,766.3	\$6,138.1

(1) The three and nine months ended September 30, 2014 include fees mandated by the ACA comprised primarily of the HIF of \$151.5 million and \$454.0 million, respectively, and our estimated contribution to the funding of the reinsurance program of \$80.5 million and \$251.6 million, respectively. Refer to Note 2 beginning on page 6 for additional information on fees mandated by the ACA.

In the fourth quarter of 2012, we recorded a charge of \$120.0 million pretax related to the settlement of purported class action litigation regarding Aetna's payment practices related to out-of-network health care providers. That charge included the estimated cost of legal fees of plaintiffs' counsel and the costs of administering the settlement.

(2) In the first quarter of 2014, we exercised our right to terminate the settlement agreement. As a result, we released the reserve established in connection with the settlement agreement, net of amounts due to the settlement administrator, which reduced first quarter 2014 other general and administrative expenses by \$103.0 million pretax. Refer to Note 13 beginning on page 30 for additional information on the termination of the settlement agreement.

In 2008, as a result of the liquidation proceedings of Lehman Re Ltd. ("Lehman Re"), a subsidiary of Lehman Brothers Holdings Inc., we recorded an allowance against our reinsurance recoverable from Lehman Re of \$42.2 million pretax. This reinsurance was placed in 1999 and was on a closed book of paid-up group whole life insurance business. In the second quarter of 2013, we sold our claim against Lehman Re to an unrelated third party (including the reinsurance recoverable) and terminated the reinsurance arrangement. Upon the sale of the claim and termination of the arrangement, we reversed the related allowance thereby reducing second quarter 2013 other general and administrative expenses by \$42.2 million pretax.

(3)

The three and nine months ended September 30, 2014 include \$35.3 million and \$154.8 million, respectively, of transaction and integration-related costs related to the acquisitions of Coventry and InterGlobal. The three and nine months ended September 30, 2013 include \$51.2 million and \$171.4 million, respectively, of transaction and integration-related costs related to the acquisition of Coventry, including advisory, legal and other professional services fees and transaction-related payments.

(4)

Refer to the reconciliation of operating earnings to net income attributable to Aetna in Note 14 beginning on page 33 for additional information.

6. Investments

Total investments at September 30, 2014 and December 31, 2013 were as follows:

(Millions)	September 30, 2014			December 31, 2013		
	Current	Long-term	Total	Current	Long-term	Total
	\$2,318.0	\$18,620.6	\$20,938.6	\$1,977.4	\$17,753.0	\$19,730.4

Debt and equity securities
available for sale

Mortgage loans	130.9	1,473.2	1,604.1	84.9	1,464.7	1,549.6
Other investments	13.1	1,777.7	1,790.8	1.5	1,717.3	1,718.8
Total investments	\$2,462.0	\$21,871.5	\$24,333.5	\$2,063.8	\$20,935.0	\$22,998.8

At September 30, 2014 and December 31, 2013, approximately \$840 million and \$766 million, respectively, of investments were pledged under securities loan agreements.

Debt and Equity Securities

Debt and equity securities available for sale at September 30, 2014 and December 31, 2013 were as follows:

(Millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2014				
Debt securities:				
U.S. government securities	\$1,364.5	\$79.0	\$(1.2)	\$1,442.3
States, municipalities and political subdivisions	4,327.5	250.5	(11.0)	4,567.0
U.S. corporate securities	7,915.7	571.4	(40.1)	8,447.0
Foreign securities	3,285.4	259.5	(13.4)	3,531.5
Residential mortgage-backed securities	913.8	22.2	(8.0)	928.0
Commercial mortgage-backed securities	1,340.3	62.6	(2.2)	1,400.7 ⁽¹⁾
Other asset-backed securities	517.9	6.4	(2.5)	521.8 ⁽¹⁾
Redeemable preferred securities	56.8	11.5	—	68.3
Total debt securities	19,721.9	1,263.1	(78.4)	20,906.6
Equity securities	37.3	.4	(5.7)	32.0
Total debt and equity securities ⁽²⁾	\$19,759.2	\$1,263.5	\$(84.1)	\$20,938.6
December 31, 2013				
Debt securities:				
U.S. government securities	\$1,396.8	\$68.7	\$(3.0)	\$1,462.5
States, municipalities and political subdivisions	4,118.5	126.6	(82.8)	4,162.3
U.S. corporate securities	7,559.0	493.7	(110.1)	7,942.6
Foreign securities	3,209.6	198.9	(53.0)	3,355.5
Residential mortgage-backed securities	928.4	16.9	(21.1)	924.2
Commercial mortgage-backed securities	1,323.5	88.2	(4.7)	1,407.0 ⁽¹⁾
Other asset-backed securities	343.4	8.3	(2.1)	349.6 ⁽¹⁾
Redeemable preferred securities	56.8	8.6	—	65.4
Total debt securities	18,936.0	1,009.9	(276.8)	19,669.1
Equity securities	38.5	26.5	(3.7)	61.3
Total debt and equity securities ⁽²⁾	\$18,974.5	\$1,036.4	\$(280.5)	\$19,730.4

At September 30, 2014 and December 31, 2013, we held securities for which we previously recognized \$18.6 million and \$22.8 million, respectively, of non-credit related impairments in accumulated other comprehensive loss. These securities had a net unrealized capital gain at September 30, 2014 and December 31, 2013 of \$4.2 million and \$6.6 million, respectively.

Investment risks associated with our experience-rated and discontinued products generally do not impact our operating results (refer to Note 16 beginning on page 35 for additional information on our accounting for discontinued products). At September 30, 2014, debt and equity securities with a fair value of approximately \$3.6 billion, gross unrealized capital gains of \$360.6 million and gross unrealized capital losses of \$20.8 million and, at December 31, 2013, debt and equity securities with a fair value of approximately \$3.7 billion, gross unrealized capital gains of \$291.3 million and gross unrealized capital losses of \$60.3 million were included in total debt and equity securities, but support our experience-rated and discontinued products. Changes in net unrealized capital gains (losses) on these securities are not reflected in accumulated other comprehensive income.

The fair value of debt securities at September 30, 2014 is shown below by contractual maturity. Actual maturities may differ from contractual maturities because securities may be restructured, called or prepaid.

(Millions)	Fair Value
Due to mature:	
Less than one year	\$1,177.9
One year through five years	5,636.2
After five years through ten years	5,693.5
Greater than ten years	5,548.5
Residential mortgage-backed securities	928.0
Commercial mortgage-backed securities	1,400.7
Other asset-backed securities	521.8
Total	\$20,906.6

Mortgage-Backed and Other Asset-Backed Securities

All of our residential mortgage-backed securities at September 30, 2014 were issued by the Government National Mortgage Association, the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation and carry agency guarantees and explicit or implicit guarantees by the U.S. Government. At September 30, 2014, our residential mortgage-backed securities had an average credit quality rating of AAA and a weighted average duration of 4.6 years.

Our commercial mortgage-backed securities have underlying loans that are dispersed throughout the United States. Significant market observable inputs used to value these securities include probability of default and loss severity. At September 30, 2014, these securities had an average credit quality rating of AA+ and a weighted average duration of 2.0 years.

Our other asset-backed securities have a variety of underlying collateral (e.g., automobile loans, credit card receivables, home equity loans and commercial loans). Significant market observable inputs used to value these securities include the unemployment rate, loss severity and probability of default. At September 30, 2014, these securities had an average credit quality rating of A+ and a weighted average duration of 1.8 years.

Unrealized Capital Losses and Net Realized Capital Gains (Losses)

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

Summarized below are the debt and equity securities we held at September 30, 2014 and December 31, 2013 that were in an unrealized capital loss position, aggregated by the length of time the investments have been in that position:

(Millions)	Less than 12 months		Greater than 12 months		Total ⁽¹⁾	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
September 30, 2014						
Debt securities:						
U.S. government securities	\$129.8	\$.5	\$27.5	\$.7	\$157.3	\$1.2
States, municipalities and political subdivisions	350.6	2.3	492.2	8.7	842.8	11.0
U.S. corporate securities	1,271.3	14.7	593.0	25.4	1,864.3	40.1
Foreign securities	441.5	6.3	181.5	7.1	623.0	13.4
Residential mortgage-backed securities	59.9	.2	205.2	7.8	265.1	8.0
Commercial mortgage-backed securities	77.4	.3	79.7	1.9	157.1	2.2
Other asset-backed securities	242.3	1.8	29.4	.7	271.7	2.5
Total debt securities	2,572.8	26.1	1,608.5	52.3	4,181.3	78.4
Equity securities	—	—	8.6	5.7	8.6	5.7
Total debt and equity securities ⁽¹⁾	\$2,572.8	\$26.1	\$1,617.1	\$58.0	\$4,189.9	\$84.1
December 31, 2013						
Debt securities:						
U.S. government securities	\$555.9	\$2.7	\$13.4	\$.3	\$569.3	\$3.0
States, municipalities and political subdivisions	1,779.9	73.1	132.4	9.7	1,912.3	82.8
U.S. corporate securities	2,196.8	88.0	170.0	22.1	2,366.8	110.1
Foreign securities	875.2	43.5	90.9	9.5	966.1	53.0
Residential mortgage-backed securities	541.1	17.3	35.0	3.8	576.1	21.1
Commercial mortgage-backed securities	162.4	4.2	25.0	.5	187.4	4.7
Other asset-backed securities	87.8	1.9	7.7	.2	95.5	2.1
Redeemable preferred securities	4.4	—	—	—	4.4	—
Total debt securities	6,203.5	230.7	474.4	46.1	6,677.9	276.8
Equity securities	—	—	16.2	3.7	16.2	3.7
Total debt and equity securities ⁽¹⁾	\$6,203.5	\$230.7	\$490.6	\$49.8	\$6,694.1	\$280.5

At September 30, 2014 and December 31, 2013, debt and equity securities in an unrealized capital loss position of ⁽¹⁾ \$20.8 million and \$60.3 million, respectively, and with related fair value of \$581.1 million and \$1.0 billion, respectively, related to experience-rated and discontinued products.

We reviewed the securities in the tables above and concluded that these are performing assets generating investment income to support the needs of our business. In performing this review, we considered factors such as the quality of the investment security based on research performed by our internal credit analysts and external rating agencies and the prospects of realizing the carrying value of the security based on the investment's current prospects for recovery. At September 30, 2014, we did not intend to sell these securities, and we did not believe it was more likely than not that we would be required to sell these securities prior to anticipated recovery of their carrying value.

The maturity dates for debt securities in an unrealized capital loss position at September 30, 2014 were as follows:

(Millions)	Supporting discontinued and experience-rated products		Supporting remaining products		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Due to mature:						
Less than one year	\$—	\$—	\$34.5	\$.4	\$34.5	\$.4
One year through five years	35.1	.3	917.7	6.6	952.8	6.9
After five years through ten years	246.3	4.7	1,243.7	22.8	1,490.0	27.5
Greater than ten years	281.1	10.0	729.0	20.9	1,010.1	30.9
Residential mortgage-backed securities	6.0	—	259.1	8.0	265.1	8.0
Commercial mortgage-backed securities	4.0	.1	153.1	2.1	157.1	2.2
Other asset-backed securities	—	—	271.7	2.5	271.7	2.5
Total	\$572.5	\$15.1	\$3,608.8	\$63.3	\$4,181.3	\$78.4

Net realized capital gains (losses) for the three and nine months ended September 30, 2014 and 2013, excluding amounts related to experience-rated contract holders and discontinued products, were as follows:

(Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
OTTI losses on debt securities recognized in earnings	\$(3.0)	\$(2.4)	\$(3.3)	\$(29.6)
Net realized capital gains (losses), excluding OTTI losses on debt securities	31.3	(10.3)	83.9	17.4
Net realized capital gains (losses)	\$28.3	\$(12.7)	\$80.6	\$(12.2)

The net realized capital gains for the three and nine months ended September 30, 2014 were primarily attributable to gains from sales of debt securities. The net realized capital gains for the nine months ended September 30, 2014 were also attributable to gains from the sales of equity securities and the recognition of a gain on the termination of interest rate swaps during the first quarter of 2014. Refer to Note 10 of Condensed Notes to Consolidated Financial Statements beginning on page 27 for more information on the termination of the outstanding interest rate swaps in the first quarter of 2014. The net realized capital losses for the three months ended September 30, 2013 were primarily attributable to losses from sales of debt securities and yield-related OTTI on debt securities. The net realized capital losses for the nine months ended September 30, 2013 were primarily attributable to yield-related OTTI on debt securities, primarily on U.S. Treasury securities, which was partially offset by gains from sales of other debt securities.

Excluding amounts related to experience-rated and discontinued products, proceeds from the sale of debt securities and the related gross realized capital gains and losses for the three and nine months ended September 30, 2014 and 2013 were as follows:

(Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Proceeds on sales	\$955.3	\$1,434.0	\$2,979.0	\$5,216.5
Gross realized capital gains	34.2	25.0	78.7	83.9
Gross realized capital losses	5.1	34.9	27.1	78.3

Mortgage Loans

Our mortgage loans are collateralized by commercial real estate. During the three and nine months ended September 30, 2014 and 2013 we had the following activity in our mortgage loan portfolio:

(Millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
New mortgage loans	\$44.1	\$62.8	\$185.0	\$126.4
Mortgage loans fully repaid	17.3	49.1	73.9	168.7

At September 30, 2014 and December 31, 2013, we had no material problem, restructured or potential problem mortgage loans. We also had no material impairment reserves on these loans at September 30, 2014 or December 31, 2013. During the three and nine months ended September 30, 2014 and 2013, we had no mortgage loans foreclosed.

We assess our mortgage loans on a regular basis for credit impairments, and annually assign a credit quality indicator to each loan. Our credit quality indicator is internally developed and categorizes our portfolio on a scale from 1 to 7. Category 1 represents loans of superior quality, and Categories 6 and 7 represent loans where collections are potentially at risk. The vast majority of our mortgage loans fall into the Level 2 to 4 ratings. These ratings represent loans where credit risk is minimal to acceptable; however, these loans may display some susceptibility to economic changes. Category 5 represents loans where credit risk is not substantial but these loans warrant management's close attention. These indicators are based upon several factors, including current loan to value ratios, property condition, market trends, creditworthiness of the borrower and deal structure. Based upon our most recent assessments at September 30, 2014 and December 31, 2013, our mortgage loans were given the following credit quality indicators:

(In Millions, except credit ratings indicator)	September 30, 2014	December 31, 2013
1	\$75.2	\$69.2
2 to 4	1,466.7	1,399.6
5	21.5	30.6
6 and 7	40.7	50.2
Total	\$1,604.1	\$1,549.6

Variable Interest Entities

In determining whether to consolidate a variable interest entity ("VIE"), we consider several factors including whether we have the power to direct activities, the obligation to absorb losses and the right to receive benefits that could potentially be significant to the VIE. We have relationships with certain real estate partnerships and one hedge fund partnership that are considered VIEs, but are not consolidated. We record the amount of our investment in these partnerships as long-term investments on our balance sheets and recognize our share of partnership income or losses in earnings. Our maximum exposure to loss as a result of our investment in these partnerships is our investment balance at September 30, 2014 and December 31, 2013 of approximately \$210 million and \$205 million, respectively, and the risk of recapture of tax credits related to the real estate partnerships previously recognized, which we do not consider significant. We do not have a future obligation to fund losses or debts on behalf of these investments; however, we may voluntarily contribute funds. The real estate partnerships construct, own and manage low-income housing developments and had total assets of approximately \$5.7 billion and \$5.8 billion at September 30, 2014 and December 31, 2013, respectively. The hedge fund partnership had total assets of approximately \$7.1 billion and \$7.0 billion at September 30, 2014 and December 31, 2013, respectively.

Non-controlling (Minority) Interests

At September 30, 2014 and December 31, 2013, continuing business non-controlling interests were approximately \$61 million and \$53 million, respectively, primarily related to third party interests in our investment holdings as well as third party interests in certain of our operating entities. The non-controlling entities' share was included in total equity. Net income attributable to non-controlling interests was \$4.3 million and \$6.6 million for the three and nine months ended September 30, 2014, respectively. Net income attributable to non-controlling interests was \$.4 million for the three months ended September 30, 2013, and net loss attributable to non-controlling interests was \$1.6 million for the nine months ended September 30, 2013. These non-controlling interests did not have a material impact on our financial position or operating results.

Net Investment Income

Sources of net investment income for the three and nine months ended September 30, 2014 and 2013 were as follows:

(Millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Debt securities	\$198.9	\$193.9	\$595.2	\$573.9
Mortgage loans	24.1	27.2	82.1	76.1
Other investments	22.5	(2.2)	) 57.9	46.8
Gross investment income	245.5	218.9	735.2	696.8
Investment expenses	(10.9)	) (8.9)	) (28.1)	) (26.7)
Net investment income ⁽¹⁾	\$234.6	\$210.0	\$707.1	\$670.1

Net investment income includes \$72.5 million and \$216.4 million for the three and nine months ended

⁽¹⁾ September 30, 2014, respectively, and \$61.5 million and \$210.3 million for the three and nine months ended September 30, 2013, respectively, related to investments supporting our experience-rated and discontinued products.

7. Other Comprehensive (Loss) Income

Shareholders' equity included the following activity in accumulated other comprehensive loss for the nine months ended September 30, 2014 and 2013:

(Millions)	Net Unrealized Gains (Losses) Securities		Foreign Currency and Derivative	Pension and OPEB Plans		Total Accumulated Other Comprehensive (Loss) Income
	Previously Impaired (1)	All Other		Unrecognized Net Actuarial Losses	Unrecognized Prior Service Credit	
Nine months ended September 30, 2014						
Balance at December 31, 2013	\$34.2	\$326.8	\$4	\$(1,293.8)	\$20.3	\$(912.1)
Other comprehensive (loss) income						
before reclassifications	(1.2)	212.5	(36.0)	—	—	175.3
Amounts reclassified from accumulated						
other comprehensive income	(.2) ^(2)	(6.2) ^(2)	(8.3) ^(3)	23.2	(2.0) ^(4)	6.5
Other comprehensive (loss) income	(1.4)	206.3	(44.3)	23.2	(2.0)	181.8
Balance at September 30, 2014	\$32.8	\$533.1	\$(43.9)	\$(1,270.6)	\$18.3	\$(730.3)
Nine months ended September 30, 2013						
Balance at December 31, 2012	\$57.3	\$825.2	\$(29.5)	\$(1,909.4)	\$23.0	\$(1,033.4)
Other comprehensive (loss) income						
before reclassifications	(40.8)	(481.1)	22.9	—	—	(499.0)
Amounts reclassified from accumulated						
other comprehensive income	20.6	17.2 ^(2)	2.6 ^(2)	37.9 ^(3)	(2.0) ^(4)	76.3
Other comprehensive (loss) income	(20.2)	(463.9)	25.5	37.9	(2.0)	(422.7)
Balance at September 30, 2013	\$37.1	\$361.3	\$(4.0)	\$(1,871.5)	\$21.0	\$(1,456.1)

(1) Represents unrealized gains on the non-credit related component of impaired debt securities that we do not intend to sell and subsequent changes in the fair value of any previously impaired security.

(2) Reclassifications out of accumulated other comprehensive income for previously impaired debt securities and all other securities are reflected in net realized capital gains (losses) within the Consolidated Statements of Income.

(3) Reclassifications out of accumulated other comprehensive income for foreign currency gains (losses) and derivatives are reflected in net realized capital gains (losses) within the Consolidated Statements of Income, except for the effective portion of derivatives related to interest rate swaps which are reflected in interest expense and were not material during the nine months ended September 30, 2014 or 2013. Refer to Note 10 of Condensed

Notes to Consolidated Financial Statements beginning on page 27 for additional information.

Reclassifications out of accumulated other comprehensive income for pension and OPEB plan expenses are⁽⁴⁾ reflected in general and administrative expenses within the Consolidated Statements of Income. Refer to Note 9 of Condensed Notes to Consolidated Financial Statements beginning on page 26 for additional information.

Refer to the Consolidated Statements of Comprehensive Income on page 2 for additional information regarding reclassifications out of accumulated other comprehensive income on a pretax basis.

8. Financial Instruments

The preparation of our consolidated financial statements in accordance with GAAP requires certain of our assets and liabilities to be reflected at their fair value, and others on another basis, such as an adjusted historical cost basis. In this note, we provide details on the fair value of financial assets and liabilities and how we determine those fair values. We present this information for those financial instruments that are measured at fair value for which the change in fair value impacts net income attributable to Aetna or other comprehensive income separately from other financial assets and liabilities.

Financial Instruments Measured at Fair Value in our Balance Sheets

Certain of our financial instruments are measured at fair value in our balance sheets. The fair values of these instruments are based on valuations that include inputs that can be classified within one of three levels of a hierarchy established by GAAP. The following are the levels of the hierarchy and a brief description of the type of valuation information (“inputs”) that qualifies a financial asset or liability for each level:

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

Level 2 – Inputs other than Level 1 that are based on observable market data. These include: quoted prices for similar assets in active markets, quoted prices for identical assets in inactive markets, inputs that are observable that are not prices (such as interest rates and credit risks) and inputs that are derived from or corroborated by observable markets.

Level 3 – Developed from unobservable data, reflecting our own assumptions.

Financial assets and liabilities are classified based upon the lowest level of input that is significant to the valuation. When quoted prices in active markets for identical assets and liabilities are available, we use these quoted market prices to determine the fair value of financial assets and liabilities and classify these assets and liabilities as Level 1. In other cases where a quoted market price for identical assets and liabilities in an active market is either not available or not observable, we estimate fair value using valuation methodologies based on available and observable market information or by using a matrix pricing model. These financial assets and liabilities would then be classified as Level 2. If quoted market prices are not available, we determine fair value using broker quotes or an internal analysis of each investment’s financial performance and cash flow projections. Thus, financial assets and liabilities may be classified as Level 3 even though there may be some significant inputs that may be observable.

The following is a description of the valuation methodologies used for our financial assets and liabilities that are measured at fair value, including the general classification of such assets and liabilities pursuant to the valuation hierarchy.

Debt Securities – Where quoted prices are available in an active market, our debt securities are classified in Level 1 of the fair value hierarchy. Our Level 1 debt securities are comprised primarily of U.S. Treasury securities.

The fair values of our Level 2 debt securities are obtained using models such as matrix pricing, which use quoted market prices of debt securities with similar characteristics, or discounted cash flows to estimate fair value. We review these prices to ensure they are based on observable market inputs that include, but are not limited to, quoted prices for similar assets in active markets, quoted prices for identical assets in inactive markets and inputs that are observable but not prices (for example, interest rates and credit risks). We also review the methodologies and the assumptions used to calculate prices from these observable inputs. On a quarterly basis, we select a sample of our Level 2 debt securities’ prices and compare them to prices provided by a secondary source. Variances over a specified threshold are identified and reviewed to confirm the price provided by the primary source represents an appropriate estimate of fair value. In addition, our internal investment team consistently compares the prices obtained for select Level 2 debt securities to the team’s own independent estimates of fair value for those securities. We obtained one price for each of our Level 2 debt securities and did not adjust any of these prices at September 30, 2014 or December 31, 2013.

We also value certain debt securities using Level 3 inputs. For Level 3 debt securities, fair values are determined by outside brokers or, in the case of certain private placement securities, are priced internally. Outside brokers determine the value of these debt securities through a combination of their knowledge of the current pricing environment and market flows. We obtained one non-binding broker quote for each of these Level 3 debt securities and did not adjust any of these quotes at September 30, 2014 or December 31, 2013. The total fair value of our broker quoted debt securities was approximately \$115 million at September 30, 2014 and \$103 million at December 31, 2013. Examples of these broker quoted Level 3 debt securities include certain U.S. and foreign corporate securities and certain of our commercial mortgage-backed securities as well as other asset-backed securities. For some of our private placement

securities, our internal staff determines the value of these debt securities by analyzing spreads of corporate and sector indices as well as interest spreads of comparable public bonds. Examples of these private placement Level 3 debt securities include certain U.S. and foreign securities and certain tax-exempt municipal securities.

Equity Securities – We currently have two classifications of equity securities: those that are publicly traded and those that are privately held. Our publicly-traded securities are classified as Level 1 because quoted prices are available for these securities in an active market. For privately-held equity securities, there is no active market; therefore, we classify these securities as Level 3 because we price these securities through an internal analysis of each investment's financial statements and cash flow projections. Significant unobservable inputs consist of earnings and revenue multiples, discount for lack of marketability and comparability adjustments. An increase or decrease in any of these unobservable inputs would result in a change in the fair value measurement, which may be significant.

Derivatives – Where quoted prices are available in an active market, our derivatives are classified as Level 1. Certain of our derivative instruments are valued using models that primarily use market observable inputs and therefore are classified as Level 2 because they are traded in markets where quoted market prices are not readily available.

Financial assets and liabilities measured at fair value on a recurring basis in our balance sheets at September 30, 2014 and December 31, 2013 were as follows:

(Millions)	Level 1	Level 2	Level 3	Total
September 30, 2014				
Assets:				
Debt securities:				
U.S. government securities	\$1,232.7	\$209.6	\$—	\$1,442.3
States, municipalities and political subdivisions	—	4,565.8	1.2	4,567.0
U.S. corporate securities	—	8,398.4	48.6	8,447.0
Foreign securities	—	3,502.8	28.7	3,531.5
Residential mortgage-backed securities	—	928.0	—	928.0
Commercial mortgage-backed securities	—	1,393.2	7.5	1,400.7
Other asset-backed securities	—	479.4	42.4	521.8
Redeemable preferred securities	—	64.2	4.1	68.3
Total debt securities	1,232.7	19,541.4	132.5	20,906.6
Equity securities	8.9	—	23.1	32.0
Derivatives	—	.2	—	.2
Total	\$1,241.6	\$19,541.6	\$155.6	\$20,938.8
Liabilities:				
Derivatives	\$—	\$38.6	\$—	\$38.6
December 31, 2013				
Assets:				
Debt securities:				
U.S. government securities	\$1,237.5	\$225.0	\$—	\$1,462.5
States, municipalities and political subdivisions	—	4,161.0	1.3	4,162.3
U.S. corporate securities	—	7,911.4	31.2	7,942.6
Foreign securities	—	3,311.6	43.9	3,355.5
Residential mortgage-backed securities	—	924.2	—	924.2
Commercial mortgage-backed securities	—	1,399.5	7.5	1,407.0
Other asset-backed securities	—	317.3	32.3	349.6
Redeemable preferred securities	—	61.3	4.1	65.4
Total debt securities	1,237.5	18,311.3	120.3	19,669.1
Equity securities	17.1	—	44.2	61.3
Derivatives	—	49.1	—	49.1
Total	\$1,254.6	\$18,360.4	\$164.5	\$19,779.5
Liabilities:				
Derivatives	\$—	\$1.9	\$—	\$1.9

There were no transfers between Levels 1 and 2 during the three or nine months ended September 30, 2014 or 2013.

The gross transfers into (out of) Level 3 during the three and nine months ended September 30, 2014 and 2013 are as follows:

(Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Gross transfers into Level 3	\$1.9	\$3.8	\$1.9	\$3.8
Gross transfers out of Level 3	(2.0	) (21.7	) (15.3	) (48.9
Net transfers out of Level 3	\$(.1	) \$(17.9	) \$(13.4	) \$(45.1

Gross transfers into and out of Level 3 during the three months ended September 30, 2014 primarily related to other asset-backed securities. Gross transfers out of Level 3 during the nine months ended September 30, 2014 primarily related to foreign debt securities, while gross transfers into Level 3 during the nine months ended September 30, 2014 primarily related to other asset-backed securities. Gross transfers out of Level 3 during the three and nine months ended September 30, 2013 primarily related to securities of states, municipalities and political subdivisions, U.S. corporate securities and foreign debt securities. The fair value of securities transferred out of Level 3 had been based on broker quotes and effective in each of the three and nine months ended September 30, 2014 and 2013 are based primarily on a matrix pricing model, which uses quoted market prices of debt securities with similar characteristics. Gross transfers into Level 3 during the three and nine months ended September 30, 2013 primarily related to foreign debt securities and were primarily due to quoted prices for certain securities no longer being available in active markets.

Financial Instruments Not Measured at Fair Value in our Balance Sheets

The following is a description of the valuation methodologies used for estimating the fair value of our financial assets and liabilities that are carried on our balance sheets at adjusted cost or contract value.

Mortgage loans: Fair values are estimated by discounting expected mortgage loan cash flows at market rates that reflect the rates at which similar loans would be made to similar borrowers. These rates reflect our assessment of the credit worthiness of the borrower and the remaining duration of the loans. The fair value estimates of mortgage loans of lower credit quality, including problem and restructured loans, are based on the estimated fair value of the underlying collateral.

Bank loans: Where fair value is determined by quoted market prices of bank loans with similar characteristics, our bank loans are classified as Level 2. For bank loans classified as Level 3, fair value is determined by outside brokers using their internal analyses through a combination of their knowledge of the current pricing environment and market flows.

Equity securities: Certain of our equity securities are carried at cost. The fair value of our cost-method investments are not estimated if there are no identified events or changes in circumstances that may have a significant adverse effect on the fair value of the investment.

Investment contract liabilities:

- With a fixed maturity: Fair value is estimated by discounting cash flows at interest rates currently being offered by, or available to, us for similar contracts.
- Without a fixed maturity: Fair value is estimated as the amount payable to the contract holder upon demand. However, we have the right under such contracts to delay payment of withdrawals that may ultimately result in paying an amount different than that determined to be payable on demand.

Long-term debt: Fair values are based on quoted market prices for the same or similar issued debt or, if no quoted market prices are available, on the current rates estimated to be available to us for debt of similar terms and remaining maturities.

The carrying value and estimated fair value classified by level of fair value hierarchy for certain of our financial instruments at September 30, 2014 and December 31, 2013 were as follows:

(Millions)	Carrying Value	Estimated Fair Value			Total
		Level 1	Level 2	Level 3	
September 30, 2014					
Assets:					
Mortgage loans	\$1,604.1	\$—	\$—	\$1,654.8	\$1,654.8
Bank loans	232.0	—	219.2	9.7	228.9
Equity securities ⁽¹⁾	30.0	N/A	N/A	N/A	N/A
Liabilities:					
Investment contract liabilities:					
With a fixed maturity	9.0	—	—	9.0	9.0
Without a fixed maturity	563.1	—	—	558.8	558.8
Long-term debt	7,838.4	—	8,452.8	—	8,452.8
December 31, 2013					
Assets:					
Mortgage loans	\$1,549.6	\$—	\$—	\$1,584.8	\$1,584.8
Bank loans	181.7	—	171.5	9.8	181.3
Liabilities:					
Investment contract liabilities:					
With a fixed maturity	8.9	—	—	8.9	8.9
Without a fixed maturity	572.3	—	—	553.2	553.2
Long-term debt	8,252.6	—	8,670.6	—	8,670.6

(1) It was not practical to estimate the fair value of the cost-method investment as it represents common stock of an unlisted company.

Separate Accounts Measured at Fair Value in our Balance Sheets

Separate Accounts assets in our Large Case Pensions business represent funds maintained to meet specific objectives of contract holders. Since contract holders bear the investment risk of these assets, a corresponding Separate Accounts liability has been established equal to the assets. These assets and liabilities are carried at fair value. Net investment income and capital gains and losses accrue directly to such contract holders. The assets of each account are legally segregated and are not subject to claims arising from our other businesses. Deposits, withdrawals, net investment income and realized and unrealized capital gains and losses on Separate Accounts assets are not reflected in our statements of income, shareholders' equity or cash flows.

Separate Accounts assets include debt and equity securities and derivative instruments. The valuation methodologies used for these assets are similar to the methodologies described beginning on page 20. Separate Accounts assets also include investments in common/collective trusts that are carried at fair value. Common/collective trusts invest in other investment funds otherwise known as the underlying funds. The Separate Accounts' interests in the common/collective trust funds are based on the fair values of the investments of the underlying funds and therefore are classified as Level 2. The assets in the underlying funds primarily consist of equity securities. Investments in common/collective trust funds are valued at their respective net asset value per share/unit on the valuation date.

Separate Accounts financial assets at September 30, 2014 and December 31, 2013 were as follows:

(Millions)	September 30, 2014				December 31, 2013			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Debt securities	\$853.4	\$2,467.3	\$3.0	\$3,323.7	\$726.4	\$2,227.0	\$.6	\$2,954.0
Equity securities	182.2	5.7	—	187.9	188.4	3.3	—	191.7
Derivatives	—	1.5	—	1.5	—	.8	—	.8
Common/collective trusts	—	637.6	—	637.6	—	710.4	—	710.4
Total ⁽¹⁾	\$1,035.6	\$3,112.1	\$3.0	\$4,150.7	\$914.8	\$2,941.5	\$.6	\$3,856.9

⁽¹⁾ Excludes \$251.1 million and \$115.6 million of cash and cash equivalents and other receivables at September 30, 2014 and December 31, 2013, respectively.

During the three and nine months ended September 30, 2014 and 2013, we had an immaterial amount of Level 3 Separate Accounts financial assets. Gross transfers of Separate Accounts financial assets out of Level 3 during the nine months ended September 30, 2013 were \$4.6 million. For the three and nine months ended September 30, 2014 and 2013, there were no transfers of Separate Accounts financial assets between Levels 1 and 2 and no transfers of Separate Accounts financial assets into or out of Level 3 except as described in the immediately preceding sentence.

Offsetting Financial Assets and Liabilities

Certain financial assets and liabilities are offset in our balance sheets or are subject to master netting arrangements or similar agreements with the applicable counterparty. Financial assets, including derivative assets, subject to offsetting and enforceable master netting arrangements as of September 30, 2014 and December 31, 2013 were as follows:

(Millions)	Gross Amounts of Recognized Assets ⁽¹⁾	Gross Amounts Not Offset in the Balance Sheets		Net Amount
		Financial Instruments	Cash Collateral Received	
September 30, 2014				
Derivatives	\$.2	\$9.8	\$—	\$10.0
Total	\$.2	\$9.8	\$—	\$10.0
December 31, 2013				
Derivatives	\$49.1	\$13.3	\$(47.1)	)\$15.3
Total	\$49.1	\$13.3	\$(47.1)	)\$15.3

⁽¹⁾ There were no amounts offset in our balance sheets at September 30, 2014 or December 31, 2013.

Financial liabilities, including derivative liabilities, subject to offsetting and enforceable master netting arrangements as of September 30, 2014 and December 31, 2013 were as follows:

(Millions)	Gross Amounts of Recognized Liabilities (1)	Gross Amounts Not Offset in the Balance Sheets		Net Amount
		Financial Instruments	Cash Collateral Paid	
September 30, 2014				
Derivatives	\$38.6	\$—	\$(38.1)	)\$ .5
Securities lending	870.3	(870.3))—	—
Total	\$908.9	\$(870.3)	)\$(38.1)	)\$ .5
December 31, 2013				
Derivatives	\$1.9	\$—	\$(.7)	)\$1.2
Securities lending	792.6	(792.6))—	—
Total	\$794.5	\$(792.6)	)\$(.7)	)\$1.2

(1) There were no amounts offset in our balance sheets at September 30, 2014 or December 31, 2013.

9. Pension and Other Postretirement Plans

Defined Benefit Retirement Plans

Components of the net periodic benefit (income) cost of our defined benefit pension plans and other postretirement employee benefit (“OPEB”) plans for the three and nine months ended September 30, 2014 and 2013 were as follows:

(Millions)	Pension Plans				OPEB Plans			
	Three Months Ended		Nine Months Ended		Three Months Ended		Nine Months Ended	
	September 30, 2014	2013	September 30, 2014	2013	September 30, 2014	2013	September 30, 2014	2013
Service cost	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—
Amortization of prior service credit	(.2)	(.1)	(.4)	(.3)	(.9)	(1.0)	(2.7)	(2.7)
Interest cost	72.1	67.9	216.3	203.6	3.0	2.8	8.9	8.3
Expected return on plan assets	(105.6)	(99.1)	(316.7)	(297.3)	(.7)	(.6)	(2.3)	(1.8)
Recognized net actuarial losses	11.7	19.0	35.0	56.6	.2	.6	.7	1.7
Net periodic benefit (income) cost	\$(22.0)	\$(12.3)	\$(65.8)	\$(37.4)	\$1.6	\$1.8	\$4.6	\$5.5

We do not expect to make a voluntary cash contribution to our tax-qualified noncontributory defined benefit pension plan (the “Aetna Pension Plan”) in 2014.

In July 2014, we announced an enhancement to the Aetna Pension Plan, whereby effective December 1, 2014, we will provide certain current and future former employees with deferred vested Aetna Pension Plan balances an election to receive a 100% lump-sum distribution. This election is a permanent addition to the Aetna Pension Plan. In addition, in July 2014, we announced a limited-time offer to certain former employees with deferred vested Aetna Pension Plan balances that they can elect a 100% lump-sum pension distribution. The limited-time offer had to be accepted by October 10, 2014, with documentation submitted by November 5, 2014, and the resulting distributions will be paid during the fourth quarter of 2014. The amount of the one-time, non-cash settlement charge, if any, associated with the

limited-time offer will be dependent upon the final acceptance rate by the eligible former employees and other factors contributing to re-measurement of the Aetna Pension Plan assets and obligations. We intend to fund the resulting distributions using existing Aetna Pension Plan assets.

10. Debt

The carrying value of our long-term debt at September 30, 2014 and December 31, 2013 was as follows:

(Millions)	September 30, 2014	December 31, 2013
Senior notes, 6.3%, due 2014 ⁽¹⁾	\$—	\$387.3
Senior notes, 6.125%, due 2015	232.1	240.6
Senior notes, 6.0%, due 2016	—	748.9
Senior notes, 5.95%, due 2017	422.3	434.2
Senior notes, 1.75%, due 2017	249.1	248.9
Senior notes, 1.5%, due 2017	498.5	498.2
Senior notes, 6.5%, due 2018	495.1	494.9
Senior notes, 2.2%, due 2019	374.7	—
Senior notes, 3.95%, due 2020	744.9	744.3
Senior notes, 5.45%, due 2021	692.0	702.3
Senior notes, 4.125%, due 2021	495.4	494.8
Senior notes, 2.75%, due 2022	986.3	985.1
Senior notes, 6.625%, due 2036	769.8	769.8
Senior notes, 6.75%, due 2037	530.7	530.6
Senior notes, 4.5%, due 2042	480.6	480.1
Senior notes, 4.125%, due 2042	492.8	492.6
Senior notes, 4.75%, due 2044	374.1	—
Total long-term debt	7,838.4	8,252.6
Less current portion of long-term debt ⁽²⁾	232.1	387.3
Total long-term debt, less current portion	\$7,606.3	\$7,865.3

(1) The 6.3% senior notes were repaid in August 2014. These notes were classified as current in the consolidated balance sheet as of December 31, 2013.

(2) At September 30, 2014, our 6.125% senior notes due January 2015 were classified as current in the accompanying consolidated balance sheet.

At September 30, 2014, we had approximately \$75 million of commercial paper outstanding with a weighted average interest rate of .21%. At December 31, 2013 we did not have any commercial paper outstanding.

Long-Term Debt and Interest Rate Swaps

On February 7, 2014, we announced the redemption for cash of the entire \$750 million aggregate principal amount outstanding of our 6.0% senior notes due 2016. The redemption of these notes occurred on March 14, 2014 (the “Redemption Date”) at a redemption price that included a make-whole premium, plus interest accrued and unpaid at the Redemption Date. We financed the redemption by issuing \$375 million of 2.2% senior notes due 2019 and \$375 million of 4.75% senior notes due 2044 (collectively, the “2014 Senior Notes”), together with other available resources. As a result of the redemption, in the first quarter of 2014, we recorded a loss on the early extinguishment of long-term debt of \$59.7 million (\$91.9 million pretax).

During June and July 2012, we entered into two interest rate swaps with an aggregate notional value of \$375 million. We designated these swaps as cash flow hedges against interest rate exposure related to the forecasted future issuance of fixed-rate debt to refinance our 6.0% senior notes due 2016. In March 2014, prior to issuing the 2014 Senior Notes used to refinance our 6.0% senior notes due 2016, we terminated these swaps and received an aggregate of \$34.2 million from the swap counterparties upon termination. We performed a final effectiveness test upon termination of these swaps and determined there was approximately \$12 million pretax of ineffectiveness that arose due to the actual

debt issuance date being earlier than forecasted. The ineffectiveness was recorded as a realized capital gain in the first quarter of 2014. The effective portion of the hedge gain of approximately \$22 million pretax was recorded in accumulated other comprehensive loss, net of tax, and is being amortized as a

reduction to interest expense over the first 20 semi-annual interest payments associated with the \$375 million of 4.75% senior notes due 2044.

In March 2014, we entered into two interest rate swaps with an aggregate notional value of \$500 million. We designated these swaps as cash flow hedges against interest rate exposure related to the forecasted future issuance of fixed-rate debt to be primarily used to refinance long-term debt maturing in 2017. At September 30, 2014, these interest rate swaps had a pretax fair value loss of \$26.8 million, which was reflected net of tax in accumulated other comprehensive loss within shareholders' equity.

In April 2014, we entered into an interest rate swap with a notional value of \$250 million. We designated this swap as a cash flow hedge against interest rate exposure related to the forecasted future issuance of fixed-rate debt to be primarily used to refinance long-term debt maturing in 2018. At September 30, 2014, this interest rate swap had a pretax fair value loss of \$11.2 million, which was reflected net of tax in accumulated other comprehensive loss within shareholders' equity.

Revolving Credit Facility

On March 27, 2012, we entered into an unsecured \$1.5 billion five-year revolving credit agreement (the "Credit Agreement") with several financial institutions. On September 24, 2012, in connection with the acquisition of Coventry, we entered into a First Amendment (the "First Amendment") to the Credit Agreement and also entered into an Incremental Commitment Agreement (the "Incremental Commitment", and together with the First Amendment and the Credit Agreement, resulting in the "Facility"). The Facility is an unsecured \$2.0 billion revolving credit agreement. Upon our agreement with one or more financial institutions, we may expand the aggregate commitments under the Facility to a maximum of \$2.5 billion. The Facility also provides for the issuance of up to \$200 million of letters of credit at our request, which count as usage of the available commitments under the Facility. In 2013, we extended the maturity date of the Facility by one year. On March 27, 2014, we extended the maturity date of the Facility by an additional year to March 27, 2019.

Various interest rate options are available under the Facility. Any revolving borrowings mature on the termination date of the Facility. We pay facility fees on the Facility ranging from .070% to .150% per annum, depending upon our long-term senior unsecured debt rating. The facility fee was .100% at September 30, 2014. The Facility contains a financial covenant that requires us to maintain a ratio of total debt to consolidated capitalization as of the end of each fiscal quarter at or below 50%. For this purpose, consolidated capitalization equals the sum of total shareholders' equity, excluding any overfunded or underfunded status of our pension and OPEB plans and any net unrealized capital gains and losses, and total debt (as defined in the Facility). We met this requirement at September 30, 2014. There were no amounts outstanding under the Facility at any time during the nine months ended September 30, 2014 or 2013.

11. Capital Stock

On February 28, 2014 and September 27, 2013, our Board of Directors (our "Board") authorized two separate share repurchase programs of our common stock of up to \$1.0 billion and \$750 million, respectively. During the nine months ended September 30, 2014, we repurchased approximately 13 million shares of common stock at a cost of approximately \$975 million. At September 30, 2014, we had remaining authorization to repurchase an aggregate of up to approximately \$622 million of common stock under the February 28, 2014 program. The repurchases are effected from time to time in the open market, through negotiated transactions, including accelerated share repurchase agreements, and through plans designed to comply with Rule 10b5-1 under the Securities Exchange Act of 1934, as amended.

Under the share repurchase program authorized by our Board, on May 16, 2014, we entered into an accelerated share repurchase agreement with an unrelated third party financial institution to repurchase an aggregate of \$100 million of our outstanding common stock during July 2014. During July 2014, we repurchased approximately 1.2 million shares of our common stock under that agreement based on the volume-weighted average price of our common stock during the purchase period.

Under the share repurchase program authorized by our Board, on August 5, 2014, we entered into an accelerated share repurchase agreement with an unrelated third party financial institution to repurchase an aggregate of \$100 million of our outstanding common stock during October 2014. The final number of shares repurchased under that agreement will be determined based on the volume-weighted average price of our common stock during the purchase period.

During the nine months ended September 30, 2014 our Board declared the following cash dividends:

Date Declared	Dividend Amount Per Share	Stockholders of Record Date	Date Paid/ To be Paid	Total Dividends (Millions)
February 28, 2014	\$.225	April 10, 2014	April 25, 2014	\$80.4
May 30, 2014	.225	July 10, 2014	July 25, 2014	79.6
September 19, 2014	.225	October 16, 2014	October 31, 2014	79.2

Declaration and payment of future dividends is at the discretion of our Board and may be adjusted as business needs or market conditions change.

On March 3, 2014, approximately .4 million PSUs, .5 million MSUs, 1.0 million restricted stock units (“RSUs”) and 1.3 million SARs were granted to certain employees. The number of vested PSUs (which could range from zero to 200% of the original number of units granted) is dependent upon the degree to which we achieve a certain operating performance goal, as determined by our Board’s Committee on Compensation and Talent Management, during a two-year performance period which began January 1, 2014 and ends on December 31, 2015. The vesting period for the PSUs ends on March 3, 2017. The number of vested MSUs (which could range from zero to 150% of the original number of units granted) is based on the percentage change between the closing price of our common stock on the grant date and the weighted average closing price of our common stock for the thirty trading days prior to and including the vesting date. The vesting period for the MSUs ends March 3, 2017. Each vested PSU, MSU and RSU represents one share of common stock and will be paid in shares of common stock, net of taxes, at the end of the applicable vesting period. The RSUs generally will become 100% vested approximately three years from the grant date, with one-third vesting each December. The SARs, if exercised by the employee, will be settled in common stock, net of taxes, based on the appreciation of our common stock price over \$72.26 per share, the closing price of our common stock on the grant date. SARs will become 100% vested approximately three years from the grant date, with one-third vesting on each anniversary of the grant date.

The SARs granted to certain employees during the first quarter of 2014 and described above had an estimated fair market value of \$22.68 per unit. The fair value per unit was calculated on the grant date using a Black-Scholes option pricing model using the following assumptions:

Expected term (in years)	5.72	
Expected volatility	35.8	%
Risk-free interest rate	1.74	%
Dividend yield	1.36	%
Initial price	\$72.26	

The expected term is based on historical equity award activity. Expected volatility is based on a weighted average of the historical volatility of our stock price and implied volatility from traded options on our stock. The risk-free interest rate is based on a U.S. Treasury rate with a life equal to the expected life of the SARs grant. This rate was calculated by interpolating between the 5-year and 10-year U.S. Treasury rates. The dividend yield is based on our historical dividends declared in the 12 months prior to the grant date.

There were no material SARs granted during the second or third quarters of 2014.

12. Dividend Restrictions and Statutory Surplus

Under applicable regulatory requirements at September 30, 2014, the amount of dividends that may be paid through the end of 2014 by our insurance and HMO subsidiaries without prior approval by regulatory authorities is approximately \$1.2 billion in the aggregate. There are no such regulatory restrictions on distributions from Aetna to its shareholders. During the third quarter of 2014, our insurance and HMO subsidiaries paid approximately \$366 million of dividends to the Company.

The combined statutory capital and surplus of our insurance and HMO subsidiaries was \$8.7 billion and \$8.4 billion at September 30, 2014 and December 31, 2013, respectively.

13. Commitments and Contingencies

Litigation and Regulatory Proceedings

Out-of-Network Benefit Proceedings

We are named as a defendant in several purported class actions and individual lawsuits arising out of our practices related to the payment of claims for services rendered to our members by health care providers with whom we do not have a contract (“out-of-network providers”). Among other things, these lawsuits allege that we paid too little to our health plan members and/or providers for these services, among other reasons, because of our use of data provided by Ingenix, Inc., a subsidiary of one of our competitors (“Ingenix”). Other major health insurers are the subject of similar litigation or have settled similar litigation.

Various plaintiffs who are health care providers or medical associations seek to represent nationwide classes of out-of-network providers who provided services to our members during the period from 2001 to the present. Various plaintiffs who are members in our health plans seek to represent nationwide classes of our members who received services from out-of-network providers during the period from 2001 to the present. Taken together, these lawsuits allege that we violated state law, the Employee Retirement Income Security Act of 1974, as amended (“ERISA”), the Racketeer Influenced and Corrupt Organizations Act and federal antitrust laws, either acting alone or in concert with our competitors. The purported classes seek reimbursement of all unpaid benefits, recalculation and repayment of deductible and coinsurance amounts, unspecified damages and treble damages, statutory penalties, injunctive and declaratory relief, plus interest, costs and attorneys’ fees, and seek to disqualify us from acting as a fiduciary of any benefit plan that is subject to ERISA. Individual lawsuits that generally contain similar allegations and seek similar relief have been brought by health plan members and out-of-network providers.

The first class action case was commenced on July 30, 2007. The federal Judicial Panel on Multi-District Litigation (the “MDL Panel”) has consolidated these class action cases in the U.S. District Court for the District of New Jersey (the “New Jersey District Court”) under the caption In re: Aetna UCR Litigation, MDL No. 2020 (“MDL 2020”). In addition, the MDL Panel has transferred the individual lawsuits to MDL 2020. On May 9, 2011, the New Jersey District Court dismissed the physician plaintiffs from MDL 2020 without prejudice. The New Jersey District Court’s action followed a ruling by the United States District Court for the Southern District of Florida (the “Florida District Court”) that the physician plaintiffs were enjoined from participating in MDL 2020 due to a prior settlement and release. The United States Court of Appeals for the Eleventh Circuit has dismissed the physician plaintiffs’ appeal of the Florida District Court’s ruling.

On December 6, 2012, we entered into an agreement to settle MDL 2020. Under the terms of the proposed nationwide settlement, we would have been released from claims relating to our out-of-network reimbursement practices from the beginning of the applicable settlement class period through August 30, 2013. The settlement agreement did not contain an admission of wrongdoing. The medical associations were not parties to the settlement agreement.

Under the settlement agreement, we would have paid up to \$120 million to fund claims submitted by health plan members and health care providers who were members of the settlement classes. These payments also would have funded the legal fees of plaintiffs' counsel and the costs of administering the settlement. In connection with the

proposed settlement, the Company recorded an after-tax charge to net income attributable to Aetna of approximately \$78 million in the fourth quarter of 2012.

The settlement agreement provided us the right to terminate the agreement under certain conditions related to settlement class members who opted out of the settlement. Based on a report provided to the parties by the settlement administrator, the conditions permitting us to terminate the settlement agreement were satisfied. On March 13, 2014, we notified the New Jersey District Court and plaintiffs' counsel that we were terminating the settlement agreement. Various legal and factual developments since the date of the settlement agreement led us to believe terminating the settlement agreement was in our best interests. We intend to vigorously defend ourselves against the claims brought by the plaintiffs. As a result of this termination, we released the reserve established in connection with the settlement agreement, net of amounts due to the settlement administrator, which reduced first quarter 2014 other general and administrative expenses by \$67.0 million (\$103.0 million pretax).

We also have received subpoenas and/or requests for documents and other information from, and been investigated by, attorneys general and other state and/or federal regulators, legislators and agencies relating to our out-of-network benefit payment and administration practices. It is reasonably possible that others could initiate additional litigation or additional regulatory action against us with respect to our out-of-network benefit payment and/or administration practices.

CMS Actions

The Centers for Medicare & Medicaid Services ("CMS") regularly audits our performance to determine our compliance with CMS's regulations and our contracts with CMS and to assess the quality of services we provide to Medicare beneficiaries. CMS uses various payment mechanisms to allocate and adjust premium payments to our and other companies' Medicare plans by considering the applicable health status of Medicare members as supported by information maintained and provided by health care providers. We collect claim and encounter data from providers and generally rely on providers to appropriately code their submissions and document their medical records. CMS pays increased premiums to Medicare Advantage plans and prescription drug program plans for members who have certain medical conditions identified with specific diagnosis codes. Federal regulators review and audit the providers' medical records to determine whether those records support the related diagnosis codes that determine the members' health status and the resulting risk-adjusted premium payments to us. In that regard, CMS has instituted risk adjustment data validation ("RADV") audits of various Medicare Advantage plans, including certain of the Company's plans. The Office of Inspector General (the "OIG") also is auditing risk adjustment data of other companies, and we expect CMS and the OIG to continue auditing risk adjustment data.

CMS is using a different audit methodology for RADV audits to determine refunds payable by Medicare Advantage plans for contract year 2011 and forward. Under this methodology, among other things, CMS will project the error rate identified in the audit sample of approximately 200 members to all risk adjusted premium payments made under the contract being audited. Historically, CMS did not project sample error rates to the entire contract. As a result, the new methodology may increase our exposure to premium refunds to CMS due to incomplete medical records maintained by providers. During 2013, CMS selected certain of our Medicare Advantage contracts for contract year 2011 for audit. We are currently unable to predict which of our Medicare Advantage contracts will be selected for future audit, the amounts of any retroactive refunds of, or prospective adjustments to, Medicare Advantage premium payments made to us, the effect of any such refunds or adjustments on the actuarial soundness of our Medicare Advantage bids, or whether any RADV audit findings would cause a change to our method of estimating future premium revenue in future bid submissions to CMS or compromise premium assumptions made in our bids for prior contract years or the current contract year. Any premium or fee refunds or adjustments resulting from regulatory audits, whether as a result of RADV or other audits by CMS, the OIG or otherwise, including audits of our minimum medical loss ratio rebates, methodology, and/or reports, could be material and could adversely affect our operating results, financial position and cash flows.

Other Litigation and Regulatory Proceedings

We are involved in numerous other lawsuits arising, for the most part, in the ordinary course of our business operations, including claims of or relating to bad faith, medical malpractice, non-compliance with state and federal

regulatory regimes, marketing misconduct, failure to timely or appropriately pay or administer claims and benefits in our Health Care and Group Insurance businesses (including our post-payment audit and collection practices and reductions in payments to providers due to sequestration), provider network structure (including the use of performance-based networks and termination of provider contracts), rescission of insurance coverage, improper disclosure of personal information, patent infringement and other intellectual property litigation, other legal proceedings in our Health Care and Group Insurance businesses and employment litigation. Some of these other lawsuits are or are purported to be class actions. We intend to vigorously defend ourselves against the claims brought in these matters.

Awards to us and others of certain government contracts, particularly in our Medicaid business, are subject to increasingly frequent protests by unsuccessful bidders. These protests may result in awards to us being reversed, delayed or modified. The loss or delay in implementation of any government contract could adversely affect our operating results. We will continue to defend vigorously contract awards we receive.

In addition, our operations, current and past business practices, current and past contracts, and accounts and other books and records are subject to routine, regular and special investigations, audits, examinations and reviews by, and from time to time we receive subpoenas and other requests for information from, CMS, the U.S. Department of Health and Human Services, various state insurance and health care regulatory authorities, state attorneys general and offices of inspector general, the Center for Consumer Information and Insurance Oversight, OIG, the Office of Personnel Management, the U.S. Department of Labor, committees, subcommittees and members of the U.S. Congress, the U.S. Department of Justice, the Federal Trade Commission, U.S. attorneys and other state, federal and international governmental authorities. These government actions include inquiries by, and testimony before, certain members, committees and subcommittees of the U.S. Congress regarding certain of our current and past business practices, including our overall claims processing and payment practices, our business practices with respect to our small group products, student health products or individual customers (such as market withdrawals, rating information, premium increases and medical benefit ratios), executive compensation matters and travel and entertainment expenses, as well as the investigations by, and subpoenas and requests from, attorneys general and others described above under “Out-of-Network Benefit Proceedings.”

Over 35 states are investigating life insurers’ claims payment and related escheat practices, and these investigations have resulted in significant charges to earnings by other life insurers in connection with related settlements. We have received requests for information from a number of states, and certain of our subsidiaries are being audited, with respect to our life insurance claim payment and related escheat practices. In the fourth quarter of 2013, we made changes to our life insurance claim payment practices (including related escheatment practices) based on evolving industry practices and regulatory expectations and interpretations, including expanding our existing use of the Social Security Administration’s Death Master File to identify additional potentially unclaimed death benefits and locate applicable beneficiaries. As a result of these changes, in the fourth quarter of 2013, we increased our estimated liability for unpaid life insurance claims with respect to insureds who passed away on or before December 31, 2013, and recorded in current and future benefits a charge of \$35.7 million (\$55.0 million pretax). Given the legal and regulatory uncertainty with respect to life insurance claim payment and related escheat practices, it is reasonably possible that we may incur additional liability related to those practices, whether as a result of further changes in our business practices, litigation, government actions or otherwise, which could adversely affect our operating results and cash flows.

There also continues to be heightened review by regulatory authorities of, and increased litigation regarding, our and the rest of the health care and related benefits industry’s business and reporting practices, including premium rate increases, utilization management, development and application of medical policies, complaint, grievance and appeal processing, information privacy, provider network structure (including the use of performance-based networks and termination of provider contracts), calculation of minimum medical loss ratios, delegated arrangements, rescission of

insurance coverage, limited benefit health products, student health products, pharmacy benefit management practices, sales practices, and claim payment practices (including payments to out-of-network providers and payments on life insurance policies).

As a leading national health and related benefits company, we regularly are the subject of government actions of the types described above. These government actions may prevent or delay us from implementing planned premium rate increases and may result, and have resulted, in restrictions on our business, changes to or clarifications of our business practices, retroactive adjustments to premiums, refunds or other payments to members, beneficiaries, states or the federal government, assessments of damages, civil or criminal fines or penalties, or other sanctions, including the possible loss of licensure or suspension or exclusion from participation in government programs.

Estimating the probable losses or a range of probable losses resulting from litigation, government actions and other legal proceedings is inherently difficult and requires an extensive degree of judgment, particularly where the matters involve indeterminate claims for monetary damages, may involve fines, penalties or punitive damages that are discretionary in amount, involve a large number of claimants or regulatory authorities, represent a change in regulatory policy, present novel legal theories, are in the early stages of the proceedings, are subject to appeal or could result in a change in business practices. In addition, because most legal proceedings are resolved over long periods of time, potential losses are subject to change due to, among other things, new developments, changes in litigation strategy, the outcome of intermediate procedural and substantive rulings and other parties' settlement posture and their evaluation of the strength or weakness of their case against us. Except as specifically noted above under "Other Litigation and Regulatory Proceedings," we are currently unable to predict the ultimate outcome of, or reasonably estimate the losses or a range of losses resulting from, the matters described above, and it is reasonably possible that their outcome could be material to us.

14. Segment Information

Our operations are conducted in three business segments: Health Care, Group Insurance and Large Case Pensions. The acquired Coventry operations are reflected in our Health Care segment for the three and nine months ended September 30, 2014 and 2013. Our Corporate Financing segment is not a business segment; it is added to our business segments to reconcile to our consolidated results. The Corporate Financing segment includes interest expense on our outstanding debt and the financing components of our pension and OPEB plan expense (the service cost and prior service cost components of this expense are allocated to our business segments). Non-GAAP financial measures we disclose, such as operating earnings, should not be considered a substitute for, or superior to, financial measures determined or calculated in accordance with GAAP.

Summarized financial information of our segments for the three and nine months ended September 30, 2014 and 2013 were as follows:

(Millions)	Health Care	Group Insurance	Large Case Pensions	Corporate Financing	Total Company
Three Months Ended September 30, 2014					
Revenue from external customers	\$13,898.4	\$559.5	\$7.0	\$—	\$14,464.9
Operating earnings (loss) ⁽¹⁾	625.6	47.9	4.9	(39.8)	) 638.6
Three Months Ended September 30, 2013					
Revenue from external customers ⁽²⁾	\$12,228.7	\$510.7	\$98.9	\$—	\$12,838.3
Operating earnings (loss) ⁽¹⁾	627.5	20.5	6.2	(49.9)	) 604.3
Nine Months Ended September 30, 2014					
Revenue from external customers	\$40,707.1	\$1,659.9	\$77.3	\$—	\$42,444.3
Operating earnings (loss) ⁽¹⁾	1,928.9	149.7	15.1	(123.1)	) 1,970.6
Nine Months Ended September 30, 2013					
Revenue from external customers ⁽²⁾	\$31,743.0	\$1,536.8	\$174.2	\$—	\$33,454.0
Operating earnings (loss) ⁽¹⁾	1,732.8	83.0	16.2	(128.6)	) 1,703.4

(1)

Operating earnings (loss) excludes net realized capital gains or losses, amortization of other acquired intangible assets and the other items described in the reconciliation below.

(2) In the third quarter of 2013, pursuant to contractual rights exercised by the contract holder, an existing group annuity contract converted from a participating to a non-participating contract. Upon conversion, we recorded \$54.1 million of non-cash group annuity conversion premium for this contract and a corresponding \$54.1 million non-cash benefit expense on group annuity conversion for this contract during the third quarter of 2013.

A reconciliation of operating earnings ⁽¹⁾ to net income attributable to Aetna for the three and nine months ended September 30, 2014 and 2013 was as follows:

(Millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Operating earnings ⁽¹⁾	\$638.6	\$604.3	\$1,970.6	\$1,703.4
Transaction and integration-related costs, net of tax	(23.7)	(34.6)	(101.9)	(140.6)
Loss on early extinguishment of long-term debt, net of tax	—	—	(59.7)	—
Release of litigation-related reserve, net of tax	—	—	67.0	—
Reduction of reserve for anticipated future losses on discontinued products, net of tax	—	—	—	55.9
Reversal of allowance and gain on sale of reinsurance recoverable, net of tax	—	—	—	32.1
Amortization of other acquired intangible assets, net of tax	(38.7)	(42.5)	(119.4)	(97.2)
Net realized capital gains (losses), net of tax	18.3	(8.6)	52.2	(8.9)
Net income attributable to Aetna	\$594.5	\$518.6	\$1,808.8	\$1,544.7

(1) In addition to net realized capital gains (losses) and amortization of other acquired intangible assets, the following other items are excluded from operating earnings because we believe they neither relate to the ordinary course of our business nor reflect our underlying business performance:

We incurred transaction and integration-related costs of \$23.7 million (\$35.3 million pretax) and \$101.9 million (\$154.8 million pretax) during the three and nine months ended September 30, 2014, respectively, related to the acquisitions of Coventry and InterGlobal, and \$34.6 million (\$51.2 million pretax) and \$140.6 million (\$189.6 million pretax) during the three and nine months ended September 30, 2013, respectively, related to the acquisition of Coventry. Transaction costs include advisory, legal and other professional fees which are not deductible for tax purposes and are reflected in our GAAP Consolidated Statements of Income in general and administrative expenses. Transaction costs also include transaction-related payments as well as expenses related to the negative cost of carry associated with the permanent financing that we obtained in November 2012 for the Coventry acquisition. Prior to the Acquisition Date, the negative cost of carry was excluded from operating earnings. The components of the negative cost of carry are reflected in our GAAP Consolidated Statements of Income in interest expense, net investment income, and general and administrative expenses. On and after the Acquisition Date, the interest expense and general and administrative expenses associated with the permanent financing are no longer excluded from operating earnings.

In the first quarter of 2014, we incurred a loss on the early extinguishment of long-term debt of \$59.7 million (\$91.9 million pretax) related to the redemption of our 6.0% senior notes due 2016.

In the fourth quarter of 2012, we recorded a charge of \$78.0 million (\$120.0 million pretax) related to the settlement of purported class action litigation regarding our payment practices related to out-of-network health care providers. That charge included the estimated cost of legal fees of plaintiffs' counsel and the costs of administering the settlement. In the first quarter of 2014, we exercised our right to terminate the settlement agreement. As a result, we released the reserve established in connection with the settlement agreement, net of amounts due to the settlement administrator, which reduced first quarter 2014 other general and administrative expenses by \$67.0 million (\$103.0 million pretax). Refer to Note 13 beginning on page 30 for additional information on the termination of the settlement agreement.

In the second quarter of 2013, we reduced the reserve for anticipated future losses on discontinued products by \$55.9 million (\$86.0 million pretax). We believe excluding any changes in the reserve for anticipated future losses on discontinued products from operating earnings provides more useful information as to our continuing products and is consistent with the treatment of the operating results of these discontinued products, which are credited or charged to

the reserve and do not affect our operating results. Refer to Note 16 beginning on page 35 for additional information on the reduction of the reserve for anticipated future losses on discontinued products.

In 2008, as a result of the liquidation proceedings of Lehman Re, a subsidiary of Lehman Brothers Holdings Inc., we recorded an allowance against our reinsurance recoverable from Lehman Re of \$27.4 million (\$42.2 million pretax). This reinsurance was placed in 1999 and was on a closed book of paid-up group whole life insurance business. In the second quarter of 2013, we sold our claim against Lehman Re to an unrelated third party (including the reinsurance recoverable) and terminated the reinsurance arrangement. Upon the sale of the claim and termination of the arrangement, we reversed the related allowance thereby reducing second quarter 2013 other general and administrative expenses by \$27.4 million (\$42.2 million pretax) and recognized a \$4.7 million (\$7.2 million pretax) gain on the sale in fees and other revenue.

15. Reinsurance

In January 2014, we entered into five-year reinsurance agreements with Vitality Re V Limited, an unrelated insurer. The agreements allow us to reduce our required capital and provide \$200 million of collateralized excess of loss reinsurance coverage on a portion of Aetna's group Commercial Insured Health Care business. The Company's similar reinsurance agreements with Vitality Re Limited and Vitality Re II Limited expired in January 2014.

16. Discontinued Products

Prior to 1993, we sold single-premium annuities ("SPAs") and guaranteed investment contracts ("GICs"), primarily to employer sponsored pension plans. In 1993, we discontinued selling these products to Large Case Pensions customers, and now we refer to these products as discontinued products.

We discontinued selling these products because they were generating losses for us, and we projected that they would continue to generate losses over their life (which is currently greater than 30 years for SPAs); so we established a reserve for anticipated future losses at the time of discontinuance. At both September 30, 2014 and December 31, 2013, our remaining GIC liability was not material. This reserve represents the present value (at the risk-free rate of return at the time of discontinuance, consistent with the duration of the liabilities) of the difference between the expected cash flows from the assets supporting these products and the cash flows expected to be required to meet the obligations of the outstanding contracts.

Key assumptions in setting the reserve for anticipated future losses include future investment results, payments to retirees, mortality and retirement rates and the cost of asset management and customer service. In 2014, we modified the mortality tables used in order to reflect the more up-to-date 2014 Retired Pensioner's Mortality table. The mortality tables were previously modified in 2012, in order to reflect the more up-to-date 2000 Retired Pensioner's Mortality table, and in 1995, in order to reflect the more up-to-date 1994 Uninsured Pensioner's Mortality table. In 1997, we began the use of a bond default assumption to reflect historical default experience. Other than these changes, since 1993 there have been no significant changes to the assumptions underlying the reserve.

We review the adequacy of this reserve quarterly based on actual experience. As long as our expected future losses remain consistent with prior projections, the results of the discontinued products are applied against the reserve and do not impact net income attributable to Aetna. If actual or expected future losses are greater than we currently estimate, we may increase the reserve, which could adversely impact net income attributable to Aetna. If actual or expected future losses are less than we currently estimate, we may decrease the reserve, which could favorably impact net income attributable to Aetna. As a result of this review, \$55.9 million (\$86.0 million pretax) of the reserve was released in the nine months ended September 30, 2013. This reserve release was primarily due to favorable investment performance as well as favorable retirement experience compared to assumptions we previously made in estimating the reserve. The reserve at each of September 30, 2014 and December 31, 2013 reflects management's best estimate of anticipated future losses, and is included in future policy benefits on our balance sheet.

The activity in the reserve for anticipated future losses on discontinued products for the nine months ended September 30, 2014 and 2013 (pretax) was as follows:

(Millions)	2014	2013
Reserve, beginning of period	\$979.5	\$978.5
Operating income (loss)	3.2	(8.5)
Net realized capital gains	25.8	73.7
Reserve reduction	—	(86.0)
Reserve, end of period	\$1,008.5	\$957.7

During the nine months ended September 30, 2014, our discontinued products reflected operating income and net realized capital gains, primarily attributable to gains from the sale of debt securities. During the nine months ended September 30, 2013, our discontinued products reflected an operating loss and net realized capital gains, primarily attributable to gains from other invested assets and from the sale of debt securities. We evaluated these results against the expectations of future cash flows assumed in estimating the reserve for anticipated future losses and did not believe that an adjustment to the reserve was required at September 30, 2014.

Assets and liabilities supporting discontinued products at September 30, 2014 and December 31, 2013 were as follows: ⁽¹⁾

(Millions)	2014	2013
Assets:		
Debt and equity securities available for sale	\$2,322.4	\$2,372.6
Mortgage loans	408.0	407.0
Other investments	675.7	663.9
Total investments	3,406.1	3,443.5
Other assets	112.3	85.2
Collateral received under securities loan agreements	222.1	204.4
Current and deferred income taxes	—	14.4
Receivable from continuing products ⁽²⁾	558.0	533.1
Total assets	\$4,298.5	\$4,280.6
Liabilities:		
Future policy benefits	\$2,685.5	\$2,804.8
Reserve for anticipated future losses on discontinued products	1,008.5	979.5
Collateral payable under securities loan agreements	222.1	204.4
Current and deferred income taxes	1.8	—
Other liabilities ⁽³⁾	380.6	291.9
Total liabilities	\$4,298.5	\$4,280.6

- ⁽¹⁾ Assets supporting the discontinued products are distinguished from assets supporting continuing products. At the time of discontinuance, a receivable from Large Case Pensions' continuing products was established on the discontinued products balance sheet. This receivable represented the net present value of anticipated cash shortfalls in the discontinued products, which will be funded from continuing products. Interest on the receivable is accrued at the discount rate that was used to calculate the reserve. The offsetting payable, on which interest is similarly accrued, is reflected in continuing products. Interest on the payable generally offsets investment income on the assets available to fund the shortfall. These amounts are eliminated in consolidation.
- ⁽²⁾ in the discontinued products, which will be funded from continuing products. Interest on the receivable is accrued at the discount rate that was used to calculate the reserve. The offsetting payable, on which interest is similarly accrued, is reflected in continuing products. Interest on the payable generally offsets investment income on the assets available to fund the shortfall. These amounts are eliminated in consolidation.
- ⁽³⁾ Net unrealized capital gains on the available-for-sale debt securities are included in other liabilities and are not reflected in consolidated shareholders' equity.

The distributions on our discontinued products consisted of scheduled contract maturities, settlements and benefit payments of \$93 million and \$284 million for the three and nine months ended September 30, 2014, respectively, and \$98 million and \$296 million for the three and nine months ended September 30, 2013, respectively. There were no material participant-directed withdrawals from our discontinued products during the three or nine months ended September 30, 2014 or 2013. Cash required to fund these distributions was provided by earnings and scheduled payments on, and sales of, invested assets.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders

Aetna Inc.:

We have reviewed the accompanying consolidated balance sheet of Aetna Inc. and subsidiaries as of September 30, 2014, the related consolidated statements of income and comprehensive income for the three and nine month periods ended September 30, 2014 and 2013, and the related consolidated statements of shareholders' equity and cash flows for the nine-month periods ended September 30, 2014 and 2013. These consolidated financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole.

Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Aetna Inc. and subsidiaries as of December 31, 2013, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated February 28, 2014, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2013, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ KPMG LLP

Hartford, Connecticut

October 28, 2014

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”)

OVERVIEW

We are one of the nation’s leading diversified health care benefits companies, serving an estimated 46 million people with information and resources to help them in consultation with their health care professionals make better informed decisions about their health care. We offer a broad range of traditional, voluntary and consumer-directed health insurance products and related services, including medical, pharmacy, dental, behavioral health, group life and disability plans, medical management capabilities, Medicaid health care management services, Medicare Advantage and Medicare supplement plans, workers’ compensation administrative services and health information technology products and services, such as Accountable Care Solutions (“ACS”). On May 7, 2013 (the “Acquisition Date”), we acquired Coventry Health Care, Inc. (“Coventry”). Our customers include employer groups, individuals, college students, part-time and hourly workers, health plans, health care providers (“providers”), governmental units, government-sponsored plans, labor groups and expatriates. Our operations are conducted in three business segments: Health Care, Group Insurance and Large Case Pensions.

The following MD&A provides a review of our financial condition at September 30, 2014 and December 31, 2013 and operating results for the three and nine months ended September 30, 2014 and 2013. The Coventry acquisition significantly impacts the comparability of our results for the nine months ended September 30, 2014 to the corresponding period in 2013 as only approximately five months of Coventry’s results were included in the corresponding period in 2013. This Overview should be read in conjunction with the entire MD&A, which contains detailed information that is important to understanding our operating results and financial condition, the consolidated financial statements and other data presented in this Quarterly Report on Form 10-Q as well as the MD&A contained in our 2013 Annual Report on Form 10-K (the “2013 Annual Report”). This Overview is qualified in its entirety by the full MD&A.

Summarized Results for the Three and Nine Months Ended September 30, 2014 and 2013:

(Millions)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Revenue:				
Health Care	\$14,012.6	\$12,299.8	\$41,044.2	\$31,970.2
Group Insurance	628.7	573.7	1,871.3	1,747.6
Large Case Pensions	86.5	162.1	316.5	394.1
Total revenue	14,727.8	13,035.6	43,232.0	34,111.9
Net income attributable to Aetna	594.5	518.6	1,808.8	1,544.7
Operating earnings: ⁽¹⁾				
Health Care	625.6	627.5	1,928.9	1,732.8
Group Insurance	47.9	20.5	149.7	83.0
Large Case Pensions	4.9	6.2	15.1	16.2
Cash flows from operations			3,078.7	1,654.6

Our discussion of operating results for our reportable business segments is based on operating earnings, which is a non-GAAP measure of net income attributable to Aetna (the term “GAAP” refers to U.S. generally accepted accounting principles). Non-GAAP financial measures we disclose, such as operating earnings, should not be ⁽¹⁾ considered a substitute for, or superior to, financial measures determined or calculated in accordance with GAAP. Refer to “Segment Results and Use of Non-GAAP Measures in this Document” beginning on page 41 for a discussion of non-GAAP measures. Refer to pages 43, 47 and 49 for a reconciliation of operating earnings to net income attributable to Aetna for Health Care, Group Insurance and Large Case Pensions, respectively.

We analyze our operating results based on operating earnings, which excludes from net income attributable to Aetna net realized capital gains and losses and amortization of other acquired intangible assets as well as other items, if any, that neither relate to the ordinary course of our business nor reflect our underlying business performance. Our operating earnings increased for the three months ended September 30, 2014 compared to the corresponding period

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in 2013 primarily as a result of higher underwriting margins (calculated as premiums less health care costs) in our Health Care segment and higher underwriting margins (calculated as premiums less current and future benefits) in our Group Insurance segment partially offset by higher general and administrative expenses due to increased investment spend to support growth, primarily in our Government business. Our operating earnings increased for the nine months ended September 30, 2014 compared to the corresponding period in 2013 primarily as a result of the May 2013 acquisition of Coventry, as well as higher underwriting margins in our Health Care and Group Insurance segments.

Total revenue increased during the three months ended September 30, 2014 compared to the corresponding period in 2013 primarily due to membership growth in our Health Care businesses and the effects of pricing actions designed to recover fees and taxes mandated by the ACA. Total revenue increased during the nine months ended September 30, 2014 compared to the corresponding period in 2013 primarily due to higher Health Care premiums from the May 2013 acquisition of Coventry, as well as membership growth in our Health Care businesses and the effects of pricing actions designed to recover fees and taxes mandated by the ACA.

At September 30, 2014, we served approximately 23.6 million medical members (consisting of approximately 40% Insured members and 60% administrative services contract (“ASC”) members), 15.4 million dental members and 15.4 million pharmacy benefit management services members. At September 30, 2013, we served approximately 22.2 million medical members (consisting of approximately 39% Insured members and 61% ASC members), 14.2 million dental members and 14.1 million pharmacy benefit management services members.

We continued to generate strong cash flows from operations in 2014 and 2013, generating \$3.3 billion and \$1.9 billion of cash flows from operations in our Health Care and Group Insurance businesses during the nine months ended September 30, 2014 and 2013, respectively. During 2014, these cash flows funded our ordinary course operating activities as well as the following:

- Repurchases of shares of our common stock of approximately \$975 million;
- The payment of our portion of the health insurer fee of approximately \$605 million in the third quarter of 2014;
- The repayment of the entire \$375 million aggregate principal amount of our 6.3% senior notes due August 2014;
- The payment of cash dividends to shareholders of approximately \$242 million; and
- The acquisition of the InterGlobal group (“InterGlobal”).

Refer to “Liquidity and Capital Resources” beginning on page 52 and Note 11 of Condensed Notes to Consolidated Financial Statements on page 28 for additional information.

Acquisition of Coventry Health Care, Inc.

On the Acquisition Date, we acquired Coventry in a transaction valued at approximately \$8.7 billion, including the \$1.8 billion fair value of Coventry’s outstanding long-term debt. We recorded goodwill related to this acquisition of approximately \$4.0 billion, of which \$267 million will be tax deductible.

Acquisition of InterGlobal

In April 2014, we acquired InterGlobal, a company that specializes in international private medical insurance for groups and individuals in the Middle East, Asia, Africa and Europe. The purchase price was not material.

Health Care Reform

The Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, “Health Care Reform” or “ACA”) has changed and will continue to make broad-based changes to the U.S. health care system which could significantly affect the U.S. economy and we expect will continue to significantly impact our business operations and financial results, including our pricing, our medical benefit ratios (“MBRs”) and the geographies in which our products are available. Health Care Reform presents us with new business opportunities, but also with new financial and regulatory challenges. It is reasonably possible that Health Care Reform, in the

aggregate, could have a material adverse effect on our business operations and financial results.

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On October 1, 2013, public health insurance exchanges (“Public Exchanges”) became available for consumers to access and begin the enrollment process for coverage beginning January 1, 2014. Through September 30, 2014, our Public Exchange membership has continued to exceed our initial projections.

In addition, because we included a portion of the 2014 Health Care Reform fees, assessments and taxes in the pricing for our 2013 contract renewals with member months in 2014, we experienced a temporary operating earnings benefit in 2013. We expect this benefit to be greatly diminished in 2014. We paid our approximately \$605 million portion of the non tax-deductible health insurer fee in September 2014. This fee is being recorded within operating expenses on a straight-line basis. In aggregate, we expect our portion of the total fees, taxes and assessments imposed by Health Care Reform to be approximately \$1.0 billion in 2014.

Federal budget negotiations, the technical problems with the federal health insurance exchange website, ongoing regulatory changes to Health Care Reform (such as the November 2013 action permitting renewal through 2014 of individual and small group insurance policies that do not comply with Health Care Reform and the March 2014 action permitting such renewal through 2017), pending efforts in the U.S. Congress to amend or restrict funding for various aspects of Health Care Reform and litigation challenging aspects of the law continue to create uncertainty about the ultimate impact of Health Care Reform. Examples of this uncertainty include the conflicting decisions issued by the United States Courts of Appeals for the District of Columbia Circuit and for the Fourth Circuit on July 22, 2014, concerning whether the Internal Revenue Service may make tax credits available as a form of subsidy to individuals who purchase health insurance through Public Exchanges established by the federal government (“Federal Exchanges”). The District of Columbia Circuit ruled that tax subsidies are only available through Public Exchanges established by the states. It is expected that one or both of these cases will be subject to further appeal or review, possibly including review by the United States Supreme Court. The District of Columbia Circuit subsequently rescinded its July 22, 2014 ruling and scheduled a rehearing of the matter by the full District of Columbia Circuit in December 2014. We will continue to enroll and insure members through the Federal Exchanges pending the resolution of these and other pending cases. If the payment of subsidies with respect to members who enroll through the Federal Exchanges ultimately is invalidated, it could result in a significant reduction in Aetna’s Public Exchange membership because almost all of Aetna’s Public Exchange membership is through Federal Exchanges, and most of those members benefit from a tax subsidy.

In May 2014, the Centers for Medicare & Medicaid Services (“CMS”) published a final rule on Public Exchanges. The final rule provides that payments to health plans under the risk corridor program required by Health Care Reform will no longer be limited to the aggregate amount of the risk corridor collections received by the U.S. Department of Health and Human Services (“HHS”) over the duration of the risk corridor program. However, it is possible that payments to health plans under the risk corridor program will require additional appropriation legislation to be passed by the U.S. Congress.

We cannot predict whether pending