UNUMPROVIDENT CORP
Form 10-Q
November 07, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

(Mark One)

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended September 30, 2006

¨ **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 1-11834

UnumProvident Corporation

(Exact name of registrant as specified in its charter)

Delaware	**62-1598430**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1 Fountain Square

Chattanooga, Tennessee 37402

(Address of principal executive offices)

423.294.1011

(Registrant s telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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 x No ¨

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

Large Accelerated Filer x Accelerated Filer ¨ Non-accelerated Filer ¨

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

As of September 30, 2006, 342,541,722 shares of the registrant s common stock were outstanding.

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Cautionary Statement Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a safe harbor to encourage companies to provide prospective information, as long as those statements are identified as forward-looking and are accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those included in the forward-looking statements. We desire to take advantage of these safe harbor provisions. Certain information contained in this discussion, or in any other written or oral statements made by us in communications with the financial community or contained in documents filed with the Securities and Exchange Commission (SEC), may be considered forward-looking. Forward-looking statements are those not based on historical information, but rather relate to future operations, strategies, financial results, or other developments and speak only as of the date made. These statements may be made directly in this document or may be made part of this document by reference to other documents filed by us with the SEC, which is known as incorporation by reference. You can find many of these statements by looking for words such as will, may, should, could, believes, expects, anticipates, estimates, inte goals, objectives, or similar expressions in this document or in documents incorporated herein.

These forward-looking statements are subject to numerous assumptions, risks, and uncertainties, many of which are beyond our control. We caution readers that the following factors, in addition to other factors mentioned from time to time, may cause actual results to differ materially from those contemplated by the forward-looking statements:

- General economic or business conditions, both domestic and foreign, may be less favorable than expected, which may affect premium levels, claims experience, the level of pension benefit costs and funding, and investment results, including credit deterioration of investments.

- Competitive pressures in the insurance industry may increase significantly through industry consolidation or otherwise.

- Events or consequences relating to terrorism and acts of war, both domestic and foreign, may adversely affect our business and the Company s results of operations in a period and may also affect the availability and cost of reinsurance.

- Legislative, regulatory, or tax changes, both domestic and foreign, may adversely affect the businesses in which we are engaged.

- Actual experience in connection with implementation of the multistate market conduct regulatory settlement agreements and the California Department of Insurance settlement agreement may deviate from our assumptions.

- Rating agency actions, state insurance department market conduct examinations and other inquiries, other governmental investigations and actions, and negative media attention may adversely affect our business and the Company s results of operations in a period.

- The level and results of litigation may vary from prior experience, rulings in the multidistrict litigation or other purported class actions may not be favorable to the Company, and either may adversely affect our business and the Company s results of operations in a period.

- Investment results, including, but not limited to, realized investment losses resulting from impairments, may differ from our assumptions and prior experience and may adversely affect our business and the Company s results of operations in a period.

- Changes in the interest rate environment may adversely affect our reserve and policy assumptions and ultimately profit margins and reserve levels.

Sales growth may be less than planned, which could affect revenue and profitability.

Effectiveness in supporting new product offerings and providing customer service may not meet expectations.

Actual experience in pricing, underwriting, and reserving may deviate from our assumptions.

Actual persistency may be lower than projected persistency, resulting in lower than expected revenue and higher than expected amortization of deferred policy acquisition costs.

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Incidence and recovery rates may be influenced by, among other factors, the rate of unemployment and consumer confidence, the emergence of new diseases, new trends and developments in medical treatments, the effectiveness of risk management programs, and implementation of the multistate regulatory settlement agreements and the California Department of Insurance settlement agreement.

Insurance reserve liabilities may fluctuate as a result of changes in numerous factors, and such fluctuations can have material positive or negative effects on net income.

Retained risks in our reinsurance operations are influenced primarily by the credit risk of the reinsurers and potential contract disputes. Any material changes in the reinsurers credit risk or willingness to pay according to the terms of the contract may adversely affect our business and the results of operations in a period.

For further discussion of risks and uncertainties which could cause actual results to differ from those contained in the forward-looking statements, see Part I, Item 1A of our annual report on Form 10-K for the year ended December 31, 2005.

All subsequent written and oral forward-looking statements attributable to the Company or any person acting on its behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We do not undertake any obligation to release publicly any revisions to such forward-looking statements to reflect events or circumstances after the date of this document or to reflect the occurrence of unanticipated events.

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PART I

ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

UnumProvident Corporation and Subsidiaries

	September 30 2006 (Unaudited)	December 31 2005
	(in millions of dollars)	
Assets		
Investments		
Fixed Maturity Securities - at fair value (amortized cost: $33,045.1; $32,062.1)	$ 34,721.3	$ 34,856.8
Mortgage Loans	893.2	739.4
Real Estate	18.0	18.2
Policy Loans	3,319.6	3,201.4
Other Long-term Investments	118.5	122.8
Short-term Investments	489.3	417.9
Total Investments	39,559.9	39,356.5
Other Assets		
Cash and Bank Deposits	32.2	69.4
Accounts and Premiums Receivable	2,041.4	1,979.2
Reinsurance Receivable	5,573.3	5,609.2
Accrued Investment Income	675.1	618.7
Deferred Policy Acquisition Costs	2,965.0	2,913.3
Value of Business Acquired	77.6	78.5
Goodwill	274.3	273.0
Property and Equipment	371.0	379.5
Current Income Tax	18.4	
Other Assets	555.3	559.9
Separate Account Assets	28.0	29.6
Total Assets	$ 52,171.5	$ 51,866.8

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION - Continued

UnumProvident Corporation and Subsidiaries

	September 30 2006 (Unaudited)	December 31 2005
	(in millions of dollars)	
Liabilities and Stockholders Equity		
Liabilities		
Policy and Contract Benefits	$ 2,193.7	$ 2,063.4
Reserves for Future Policy and Contract Benefits	35,109.5	34,041.5
Unearned Premiums	560.7	481.8
Other Policyholders Funds	2,060.4	2,235.5
Current Income Tax		18.3
Deferred Income Tax	730.8	989.7
Long-term Debt	2,561.6	3,261.6
Other Liabilities	1,332.4	1,381.5
Separate Account Liabilities	28.0	29.6
Total Liabilities	44,577.1	44,502.9
Commitments and Contingent Liabilities - Note 9		
Stockholders Equity		
Common Stock, $0.10 par		
Authorized: 725,000,000 shares		
Issued: 344,492,817 and 300,508,859 shares	34.4	30.1
Additional Paid-in Capital	2,195.5	1,627.9
Accumulated Other Comprehensive Income (Loss)		
Net Unrealized Gain on Securities	687.9	1,040.7
Net Gain on Cash Flow Hedges	181.1	273.3
Foreign Currency Translation Adjustment	47.4	22.4
Minimum Pension Liability Adjustment	(172.9)	(172.9)
Retained Earnings	4,675.2	4,610.4
Treasury Stock - at cost: 1,951,095 shares	(54.2)	(54.2)
Deferred Compensation		(13.8)
Total Stockholders Equity	7,594.4	7,363.9
Total Liabilities and Stockholders Equity	$ 52,171.5	$ 51,866.8

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

UnumProvident Corporation and Subsidiaries

	Three Months Ended September 30		Nine Months Ended September 30	
	2006	2005	2006	2005
	(in millions of dollars, except share data)			
Revenue				
Premium Income	$ 1,969.0	$ 1,952.2	$ 5,926.2	$ 5,827.2
Net Investment Income	578.8	547.2	1,719.2	1,623.4
Net Realized Investment Gain (Loss)	4.8	(71.4)	1.5	(9.1)
Other Income	110.4	115.9	330.0	331.0
Total Revenue	2,663.0	2,543.9	7,976.9	7,772.5
Benefits and Expenses				
Benefits and Change in Reserves for Future Benefits	2,088.9	1,812.1	5,764.3	5,280.6
Commissions	198.9	191.5	613.5	609.4
Interest and Debt Expense	44.2	49.8	146.0	155.5
Cost Related to Early Retirement of Debt			23.1	
Deferral of Policy Acquisition Costs	(127.5)	(119.5)	(392.8)	(402.1)
Amortization of Deferred Policy Acquisition Costs	115.9	112.5	353.7	349.4
Amortization of Value of Business Acquired	2.1	3.9	6.0	11.9
Compensation Expense	193.9	187.7	577.1	565.3
Other Operating Expenses	241.2	237.6	676.7	686.8
Total Benefits and Expenses	2,757.6	2,475.6	7,767.6	7,256.8
Income (Loss) Before Income Tax	(94.6)	68.3	209.3	515.7
Income Tax (Benefit)				
Current	9.6	44.1	104.3	87.0
Deferred	(40.5)	(28.4)	(29.9)	52.6
Total Income Tax (Benefit)	(30.9)	15.7	74.4	139.6
Net Income (Loss)	$ (63.7)	52.6	$ 134.9	$ 376.1
Net Income (Loss) Per Common Share				
Basic	$ (0.19)	$ 0.18	$ 0.42	$ 1.27
Assuming Dilution	$ (0.19)	$ 0.17	$ 0.41	$ 1.21
Dividends Paid	$ 0.075	$ 0.075	$ 0.225	$ 0.225

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY (UNAUDITED)

UnumProvident Corporation and Subsidiaries

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Retained Earnings	Treasury Stock	Deferred Compensation	Total
			(in millions of dollars)				
Balance at December 31, 2004	$ 29.8	$ 1,588.4	$ 1,481.1	$ 4,185.5	$ (54.2)	$ (6.5)	$ 7,224.1
Comprehensive Income, Net of Tax							
Net Income				376.1			376.1
Change in Net Unrealized Gain on Securities			(304.6)				(304.6)
Change in Net Gain on Cash Flow Hedges			48.1				48.1
Change in Foreign Currency Translation Adjustment			(57.6)				(57.6)
Total Comprehensive Income							62.0
Common Stock Activity	0.2	29.1				(11.2)	18.1
Dividends to Stockholders				(66.5)			(66.5)
Balance at September 30, 2005	$ 30.0	$ 1,617.5	$ 1,167.0	$ 4,495.1	$ (54.2)	$ (17.7)	$ 7,237.7
Balance at December 31, 2005	$ 30.1	$ 1,627.9	$ 1,163.5	$ 4,610.4	$ (54.2)	$ (13.8)	$ 7,363.9
Comprehensive Loss, Net of Tax							
Net Income				134.9			134.9
Change in Net Unrealized Gain on Securities			(352.8)				(352.8)
Change in Net Gain on Cash Flow Hedges			(92.2)				(92.2)
Change in Foreign Currency Translation Adjustment			25.0				25.0
Total Comprehensive Loss							(285.1)
Common Stock Activity	4.3	581.4					585.7
Reclassification Due to Accounting Principle Change		(13.8)				13.8	
Dividends to Stockholders				(70.1)			(70.1)
Balance at September 30, 2006	$ 34.4	$ 2,195.5	$ 743.5	$ 4,675.2	$ (54.2)	$	$ 7,594.4

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

UnumProvident Corporation and Subsidiaries

	Nine Months Ended September 30	
	2006	**2005**
	(in millions of dollars)	
Cash Flows from Operating Activities		
Net Income	$ 134.9	$ 376.1
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities		
Change in Receivables	3.0	20.2
Change in Deferred Policy Acquisition Costs	(39.1)	(52.7)
Change in Insurance Reserves and Liabilities	1,117.5	833.2
Change in Income Tax Liabilities	(73.3)	51.1
Change in Other Accrued Liabilities	(80.9)	(36.3)
Non-cash Adjustments to Net Investment Income	(302.2)	(313.2)
Net Realized Investment (Gain) Loss	(1.5)	9.1
Amortization of Value of Business Acquired	6.0	11.9
Depreciation	52.5	49.1
Other, Net	34.3	(2.0)
Net Cash Provided by Operating Activities	851.2	946.5
Cash Flows from Investing Activities		
Proceeds from Sales of Available-for-Sale Securities	1,760.8	1,392.1
Proceeds from Maturities of Available-for-Sale Securities	954.9	873.8
Proceeds from Sales and Maturities of Other Investments	112.2	121.5
Purchase of Available-for-Sale Securities	(3,014.8)	(3,011.4)
Purchase of Other Investments	(373.5)	(254.8)
Net Sales (Purchases) of Short-term Investments	(65.9)	112.9
Acquisition of Business		(3.5)
Disposition of Business		8.8
Other, Net	(41.0)	54.6
Net Cash Used by Investing Activities	(667.3)	(706.0)
Cash Flows from Financing Activities		
Deposits to Policyholder Accounts	1.5	2.3
Maturities and Benefit Payments from Policyholder Accounts	(6.3)	(6.4)
Short-term Debt Repayments		(227.0)
Long-term Debt Repayments	(700.0)	
Cost Related to Early Retirement of Debt	(15.6)	
Issuance of Common Stock	579.2	8.0
Dividends Paid to Stockholders	(70.1)	(66.5)
Other, Net	(10.0)	(15.9)
Net Cash Used by Financing Activities	(221.3)	(305.5)
Effect of Foreign Exchange Rate Changes on Cash	0.2	(2.0)

Net Decrease in Cash and Bank Deposits		(37.2)		(67.0)
Cash and Bank Deposits at Beginning of Year		69.4		130.7
Cash and Bank Deposits at End of Period	$	32.2	$	63.7

See notes to consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 1 - Basis of Presentation

The accompanying consolidated financial statements of UnumProvident Corporation (UnumProvident) and its subsidiaries (collectively with UnumProvident referred to as the Company) have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the consolidated financial statements and footnotes included in our annual report on Form 10-K for the year ended December 31, 2005.

In our opinion, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine month periods ended September 30, 2006, are not necessarily indicative of the results that may be expected for the year ended December 31, 2006.

Note 2 - Accounting Pronouncements

Accounting Pronouncements Adopted:

Effective January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123 (revised 2004) (SFAS 123(R)), *Share-Based Payment*, which is a revision to Statement of Financial Accounting Standards No. 123 (SFAS 123), *Accounting for Stock-Based Compensation*. SFAS 123(R) focuses primarily on accounting for transactions in which an entity obtains employee service in exchange for share-based payments. Under SFAS 123(R), share-based awards that do not require future service (i.e., vesting awards) are expensed immediately. Share-based employee awards that require future service are amortized over the relevant service period. We adopted SFAS 123(R) using the modified prospective transition method. In accordance with the modified prospective transition method, the provisions are generally applied only to share-based awards granted subsequent to adoption. The adoption of SFAS 123(R) did not have a material effect on our financial position or results of operations.

Effective January 1, 2006, we adopted the provisions of Financial Accounting Standards Board (FASB) Staff Position No. FAS 115-1 (FSP 115-1), *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, which addresses the determination of when an investment is considered impaired, whether the impairment is other than temporary, and the measurement of an impairment loss. FSP 115-1 also includes accounting considerations subsequent to the recognition of other-than-temporary impairment and requires certain disclosures about unrealized losses. The adoption of FSP 115-1 did not have a material effect on our financial position or results of operations.

Accounting Pronouncements Outstanding:

Statement of Position 05-1 (SOP 05-1), *Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection With Modifications or Exchanges of Insurance Contracts*, was issued by the Accounting Standards Executive Committee in September 2005. SOP 05-1 provides guidance on accounting by insurance enterprises for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in Statement of Financial Accounting Standards No. 97, *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments.* SOP 05-1 is effective for internal replacements occurring in fiscal years beginning after December 15, 2006, with earlier adoption encouraged. We will adopt the provisions of SOP 05-1 effective January 1, 2007. We have not yet determined the effect of the adoption of SOP 05-1 on our financial position or results of operations.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 2 - Accounting Pronouncements - Continued

Statement of Financial Accounting Standards No. 155 (SFAS 155), *Accounting for Certain Hybrid Financial Instruments, an amendment of Statement of Financial Accounting Standards Nos. 133 (SFAS 133) and 140 (SFAS 140)*, was issued in February 2006. SFAS 155: (a) permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation; (b) clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS 133; (c) establishes a requirement to evaluate beneficial interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; (d) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and, (e) eliminates restrictions on a qualifying special-purpose entity s ability to hold passive derivative financial instruments that pertain to beneficial interests that are or contain a derivative financial instrument. We will adopt the provisions of SFAS 155 effective January 1, 2007. The adoption of SFAS 155 will not have a material effect on our financial position or results of operations.

FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes, an interpretation of Statement of Financial Accounting Standard No. 109 (SFAS 109)*, was issued in June 2006. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS 109. Unlike SFAS 109, FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Additionally, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. We will adopt the provisions of FIN 48 effective January 1, 2007. We have not yet determined the effect of the adoption of FIN 48 on our financial position or results of operations.

Statement of Financial Accounting Standards No. 157 (SFAS 157), *Fair Value Measurements*, was issued in September 2006. SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. We will adopt the provisions of SFAS 157 effective January 1, 2008. The adoption of SFAS 157 will not have a material effect on our financial position or results of operations.

Statement of Financial Accounting Standards No. 158 (SFAS 158), *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans*, was issued in September 2006. SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statements of financial condition and to recognize changes in that funded status through comprehensive income. Also, under SFAS 158, defined benefit plan assets and obligations are to be measured as of the date of the employer s fiscal year-end. We will adopt the provisions of SFAS 158 effective December 31, 2006. We have not yet determined the effect of the adoption of SFAS 158 on our financial position. The adoption of SFAS 158 will have no effect on our results of operations.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 3 - Segment Information

Selected data by segment is as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2006	**2005**	**2006**	**2005**
	(in millions of dollars)			
Premium Income				
U.S. Brokerage				
Group Income Protection				
Group Long-term Income Protection	$ 484.4	$ 486.0	$ 1,459.5	$ 1,468.4
Group Short-term Income Protection	131.3	140.0	398.9	429.8
Group Life and Accidental Death & Dismemberment				
Group Life	294.5	318.3	937.1	980.5
Accidental Death & Dismemberment	36.1	37.6	113.8	116.6
Supplemental and Voluntary				
Individual Income Protection Recently Issued	111.2	106.8	332.6	321.5
Long-term Care	124.1	119.1	365.9	351.0
Voluntary Workplace Benefits	97.0	85.7	286.2	252.2
	1,278.6	1,293.5	3,894.0	3,920.0
Unum Limited				
Group Long-term Income Protection	169.5	152.4	467.2	433.4
Group Life	41.9	43.9	120.6	123.0
Individual Income Protection	8.3	7.7	24.0	30.7
	219.7	204.0	611.8	587.1
Colonial				
Income Protection	134.3	127.7	396.9	379.8
Life	33.2	28.5	95.7	84.8
Cancer and Critical Illness	45.3	41.2	132.3	121.9
	212.8	197.4	624.9	586.5
Individual Income Protection Closed Block	257.8	257.6	793.0	732.4
Other	0.1	(0.3)	2.5	1.2
	1,969.0	1,952.2	5,926.2	5,827.2

Net Investment Income and Other Income

U.S. Brokerage	289.2	276.2	859.3	822.8
Unum Limited	45.8	44.9	123.7	122.6
Colonial	23.8	24.7	70.5	75.2
Individual Income Protection Closed Block	232.5	218.6	698.9	632.7
Other	81.9	81.8	247.8	250.2
Corporate	16.0	16.9	49.0	50.9
	689.2	663.1	2,049.2	1,954.4

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 3 - Segment Information - Continued

	Three Months Ended September 30		Nine Months Ended September 30	
	2006	2005	2006	2005
	(in millions of dollars)			
Operating Revenue (Excluding Net Realized Investment Gains and Losses)				
U.S. Brokerage	$ 1,567.8	$ 1,569.7	$ 4,753.3	$ 4,742.8
Unum Limited	265.5	248.9	735.5	709.7
Colonial	236.6	222.1	695.4	661.7
Individual Income Protection Closed Block	490.3	476.2	1,491.9	1,365.1
Other	82.0	81.5	250.3	251.4
Corporate	16.0	16.9	49.0	50.9
	2,658.2	2,615.3	7,975.4	7,781.6
Benefits and Expenses				
U.S. Brokerage	1,741.0	1,497.8	4,793.5	4,459.0
Unum Limited	200.0	199.1	559.5	571.3
Colonial	184.5	180.1	547.2	532.3
Individual Income Protection Closed Block	495.6	480.8	1,449.3	1,318.9
Other	71.4	67.9	222.8	214.6
Corporate	65.1	49.9	195.3	160.7
	2,757.6	2,475.6	7,767.6	7,256.8
Operating Income (Loss) Before Income Tax and Net Realized Investment Gains and Losses				
U.S. Brokerage	(173.2)	71.9	(40.2)	283.8
Unum Limited	65.5	49.8	176.0	138.4
Colonial	52.1	42.0	148.2	129.4
Individual Income Protection Closed Block	(5.3)	(4.6)	42.6	46.2
Other	10.6	13.6	27.5	36.8
Corporate	(49.1)	(33.0)	(146.3)	(109.8)
	$ (99.4)	$ 139.7	$ 207.8	$ 524.8

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 3 - Segment Information - Continued

A reconciliation of total operating revenue and operating income (loss) by segment to revenue and net income (loss) as reported in our consolidated statements of operations is as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2006	2005	2006	2005
	(in millions of dollars)			
Operating Revenue by Segment	$ 2,658.2	$ 2,615.3	$ 7,975.4	$ 7,781.6
Net Realized Investment Gain (Loss)	4.8	(71.4)	1.5	(9.1)
Revenue	$ 2,663.0	$ 2,543.9	$ 7,976.9	$ 7,772.5
Operating Income (Loss) by Segment	$ (99.4)	$ 139.7	$ 207.8	$ 524.8
Net Realized Investment Gain (Loss)	4.8	(71.4)	1.5	(9.1)
Income Tax (Benefit)	(30.9)	15.7	74.4	139.6
Net Income (Loss)	$ (63.7)	$ 52.6	$ 134.9	$ 376.1

Assets by segment are as follows:

	September 30	December 31
	2006	2005
	(in millions of dollars)	
U.S. Brokerage	$ 20,755.1	$ 20,186.1
Unum Limited	3,819.6	3,335.3
Colonial	2,311.1	2,231.6
Individual Income Protection Closed Block	15,630.6	15,792.1
Other	9,058.1	9,143.5
Corporate	597.0	1,178.2
Total	$ 52,171.5	$ 51,866.8

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 4 - Accounting for Stock-Based Compensation

We have various stock-based employee compensation plans, as described in our annual report on Form 10-K for the year ended December 31, 2005.

Prior to 2003, we accounted for those plans under the recognition and measurement principles of Accounting Principles Board Opinion No. 25 (Opinion 25), *Accounting for Stock Issued to Employees*, and related Interpretations. All options granted prior to 2003 under the stock-based employee compensation plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

During 2003, we adopted the fair value recognition provisions of SFAS 123 and selected the prospective method of adoption allowed under the provisions of Statement of Financial Accounting Standards No. 148 (SFAS 148), *Accounting for Stock-Based Compensation Transition and Disclosure*. The recognition provisions were applied to all employee awards granted, modified, or settled after January 1, 2003.

Had we applied the fair value recognition provisions of SFAS 123 as of its original effective date, it would have reduced our net income for the nine months ended September 30, 2005 by $0.5 million, from $376.1 million to $375.6 million. There would have been no change in our reported net income per share for either the three months or nine months ended September 30, 2005, nor would there have been any change in expense recognized for the three months ended September 30, 2005.

Nonvested Stock

Compensation cost recognized for nonvested stock awards to employees was $3.3 million ($2.1 million after tax) for the three months ended September 30, 2006 and 2005. For the nine months ended September 30, 2006 and 2005, compensation cost recognized for nonvested stock awards to employees was $11.9 million and $8.6 million ($7.7 million and $5.6 million after tax), respectively. The weighted average grant date fair values for nonvested stock awards granted in the first nine months of 2006 and 2005 were $20.95 and $17.43, respectively.

Nonvested shares vest over a two to five year service period commencing upon the date of grant, and the compensation cost is recognized ratably during the vesting period. Compensation cost for stock awards subject to accelerated vesting upon retirement is recognized over the implicit service period for grants issued subsequent to 2005 and over the explicit service period (subject to acceleration upon actual retirement) for grants issued prior to 2006. We pay cash dividend equivalents on outstanding nonvested stock. Dividend equivalents paid on nonvested stock are charged to retained earnings when paid. At September 30, 2006, we had $24.3 million of unrecognized compensation cost related to nonvested stock that will be recognized over a weighted average period of 1.3 years. Prior to the adoption of SFAS 123(R), this amount was reported as additional paid-in capital and deferred compensation, a contra equity account. The value of this contra equity account at the adoption of SFAS 123(R) was $13.8 million.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 4 - Accounting for Stock-Based Compensation - Continued

Nonvested share activity under the plans for the first nine months of 2006 is summarized as follows:

	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2005	2,187,284	$ 14.61
Granted	780,931	20.95
Vested	(1,049,710)	11.90
Forfeited	(71,133)	18.53
Nonvested at September 30, 2006	1,847,372	18.69

Stock Options

Compensation cost recognized for stock options was immaterial for the three and nine months ended September 30, 2006 and 2005. We issue new shares upon the exercise of an option.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 5 - Pensions and Other Postretirement Benefits

The components of net periodic benefit cost related to the Company sponsored defined benefit pension and postretirement plans for our employees are as follows:

	U.S. Plans Pension Benefits		Non-U.S. Plans Pension Benefits		Postretirement Benefits	
	Three Months Ended September 30					
	2006	2005	2006	2005	2006	2005
	(in millions of dollars)					
Service Cost	$ 9.0	$ 8.8	$ 2.3	$ 2.3	$ 1.0	$ 1.0
Interest Cost	12.1	10.9	2.0	1.9	2.5	2.6
Expected Return on Plan Assets	(11.0)	(10.0)	(2.8)	(1.7)	(0.1)	(0.1)
Amortization of Prior Service Cost	(0.8)	(0.7)			(1.0)	(1.0)
Amortization of Net Loss	5.6	4.8	0.6	0.7		
Net Periodic Benefit Cost	$ 14.9	$ 13.8	$ 2.1	$ 3.2	$ 2.4	$ 2.5

	U.S. Plans Pension Benefits		Non-U.S. Plans Pension Benefits		Postretirement Benefits	
	Nine Months Ended September 30					
	2006	2005	2006	2005	2006	2005
	(in millions of dollars)					
Service Cost	$ 26.8	$ 26.4	$ 6.7	$ 6.9	$ 3.0	$ 3.1
Interest Cost	36.3	32.7	5.8	5.7	7.5	7.8
Expected Return on Plan Assets	(31.4)	(30.1)	(8.1)	(5.1)	(0.3)	(0.4)
Amortization of Prior Service Cost	(2.2)	(2.1)			(3.0)	(3.0)
Amortization of Net Loss	16.8	14.4	1.8	2.1		
Net Periodic Benefit Cost	$ 46.3	$ 41.3	$ 6.2	$ 9.6	$ 7.2	$ 7.5

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Medicare Act) was enacted in December 2003 to add a voluntary prescription drug benefit for Medicare-eligible retirees to be effective January 1, 2006. The Medicare Act allows an employer to choose whether to coordinate prescription drug benefits under a retiree medical plan with the Medicare prescription drug benefit or to keep the company plan design as it is and receive a subsidy from the federal government. We reviewed the options available as a result of Medicare reform and aligned the options, as appropriate, for each of our designated groups of retirees.

During 2005 we confirmed, using final regulations issued by the Centers for Medicare & Medicaid Services on January 21, 2005, that all of our retiree medical plans would qualify for a government subsidy under the Medicare Act and chose to defer coordination with the new prescription drug benefit until 2007. For 2006, we will maintain our current retiree medical plans and expect to receive the government subsidy for all retirees. This change is reflected in the net periodic benefit cost.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 5 - Pensions and Other Postretirement Benefits - Continued

We have no regulatory contribution requirements for our U.S. qualified defined benefit plan in 2006, but made voluntary contributions of $42.0 million in the second quarter of 2006 and $50.0 million in the third quarter of 2006. We made a $44.2 million voluntary contribution to the defined benefit plan for our U.K. operation, which maintains a separate plan, in January 2006 and additional required contributions of approximately $6.5 million during 2006.

Note 6 - Debt

In June 2006, pursuant to a cash tender offer, we purchased $50.0 million of our outstanding 7.405% capital securities due 2038 and $250.0 million aggregate principal amount of our outstanding 7.625% notes due 2011. The cost of the cash tender offer decreased second quarter and first nine months 2006 income by $17.8 million before tax, or $11.6 million after tax.

In May 2003, UnumProvident issued 23.0 million 8.25% adjustable conversion-rate equity security units (units) in a public offering for $575.0 million. Each unit had a stated amount of $25 and initially consisted of (a) a contract pursuant to which the holder agreed to purchase, for $25, shares of UnumProvident s common stock on May 15, 2006 and which entitled the holder to contract adjustment payments at the annual rate of 2.25 percent, payable quarterly, and (b) a 1/40, or 2.5 percent, ownership interest in a senior note issued by UnumProvident due May 15, 2008 with a principal amount of $1,000, on which we paid interest at the initial annual rate of 6.00 percent, payable quarterly. The scheduled remarketing of the senior note element of these units occurred in February 2006, as stipulated by the terms of the original offering, and we reset the interest rate on $575.0 million of senior notes due May 15, 2008 to 5.997%. We purchased $400.0 million of the senior notes in the remarketing which were subsequently retired. The associated write-off of deferred debt costs decreased first quarter and first nine months 2006 income by $5.3 million before tax, or $3.4 million after tax.

Upon settlement of the common stock purchase contract in May 2006, we received proceeds of approximately $575.0 million and issued 43.3 million shares of common stock.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

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September 30, 2006

Note 7 - Stockholders Equity and Earnings Per Common Share

Net income (loss) per common share is determined as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2006	2005	2006	2005
	(in millions of dollars, except share data)			
Numerator				
Net Income (Loss)	$ (63.7)	$ 52.6	$ 134.9	$ 376.1
Denominator (000s)				
Weighted Average Common Shares - Basic	340,727.7	295,767.2	319,209.4	295,628.6
Dilution for the Purchase Contract Element of the Adjustable Conversion-Rate Equity Security Units		16,156.4	9,868.5	12,432.5
Dilution for Assumed Exercises of Stock Options and Other Dilutive Securities		2,724.5	2,234.6	2,398.3
Weighted Average Common Shares - Assuming Dilution	340,727.7	314,648.1	331,312.5	310,459.4
Net Income (Loss) Per Common Share				
Basic	$ (0.19)	$ 0.18	$ 0.42	$ 1.27
Assuming Dilution	$ (0.19)	$ 0.17	$ 0.41	$ 1.21

We account for the effect of the purchase contract element of the units, outstanding stock options, and other dilutive securities on the number of weighted average common shares, assuming dilution, using the treasury stock method. Under this method, the purchase contract element of the units, outstanding stock options, and other dilutive securities will have a dilutive effect only when the average market price of UnumProvident s common stock during the period exceeds the threshold appreciation price of the purchase contract element of the units or the exercise price of the stock options. The purchase contract elements of the units issued in 2004 have a threshold appreciation price of $16.95 per share. The units issued in 2003 had a threshold appreciation price of $13.27. We settled the purchase contract element of these units in May 2006 and issued 43.3 million shares of common stock. The outstanding stock options and other dilutive securities have exercise prices ranging from $12.23 to $58.56.

In computing earnings per share assuming dilution, only potential common shares that are dilutive (those that reduce earnings per share) are included. Potential common shares are not used when computing earnings per share assuming dilution if the results would be antidilutive, such as when a net loss is reported. For the three month period ended September 30, 2006, approximately 0.9 million issuable shares related to the purchase contract elements of the units and approximately 2.3 million issuable common shares for the assumed exercises of stock options and other dilutive securities were not used in the calculation of earnings per share due to the antidilutive effect when a net loss is reported.

Options to purchase approximately 8.2 million and 8.3 million shares of common stock for the three and nine month periods ended September 30, 2006, and approximately 12.1 million and 12.4 million shares for the three and nine month periods ended September 30, 2005, were outstanding during the respective periods but were not included in the computation of earnings per common share, assuming dilution, because the exercise prices of the options were greater than the average market price of UnumProvident s common stock.

UnumProvident has 25,000,000 shares of preferred stock authorized with a par value of $0.10 per share. No preferred stock has been issued to date.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

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September 30, 2006

Note 8 - Comprehensive Income (Loss)

The components of comprehensive income (loss) and the related deferred tax are as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2006	2005	2006	2005
	(in millions of dollars)			
Net Income (Loss)	$ (63.7)	$ 52.6	$ 134.9	$ 376.1
Change in Net Unrealized Gain on Securities:				
Change Before Reclassification Adjustment	969.0	(831.1)	(535.0)	(490.9)
Reclassification Adjustment for Net Realized Investment (Gain) Loss	(2.0)	(0.4)	(5.6)	20.6
Change in Net Gain on Cash Flow Hedges	84.5	(153.5)	(141.8)	74.1
Change in Foreign Currency Translation Adjustment	9.7	(10.5)	24.8	(57.4)
	1,061.2	(995.5)	(657.6)	(453.6)
Change in Deferred Tax	369.4	(342.0)	(237.6)	(139.5)
Other Comprehensive Income (Loss)	691.8	(653.5)	(420.0)	(314.1)
Comprehensive Income (Loss)	$ 628.1	$ (600.9)	$ (285.1)	$ 62.0

Note 9 - Commitments and Contingent Liabilities

We are a defendant in a number of litigation matters. In some of these matters, no specified amount is sought. In others, very large or indeterminate amounts, including punitive and treble damages, are asserted. There is a wide variation of pleading practice permitted in the United States courts with respect to requests for monetary damages, including some courts in which no specified amount is required and others which allow the plaintiff to state only that the amount sought is sufficient to invoke the jurisdiction of that court. Further, some jurisdictions permit plaintiffs to allege damages well in excess of reasonably possible verdicts. Based on our extensive experience and that of others in the industry with respect to litigating or resolving claims through settlement over an extended period of time, we believe that the monetary damages asserted in a lawsuit or claim bear little relation to the merits of the case, or the likely disposition value. Therefore, the specific monetary relief sought is not stated.

The lawsuits described below are for the most part in very preliminary stages. The outcome of the matters is uncertain, and we are unable to estimate a range of reasonably possible losses. Unless indicated otherwise, reserves have not been established for these matters. An adverse outcome in one or more of these actions could, depending on the nature, scope, and amount of the ruling, materially adversely affect our consolidated results of operations in a period, encourage other litigation, harm the Company s reputation and goodwill, and limit our ability to write new business, particularly if the adverse outcomes negatively impact certain of our debt and financial strength ratings.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 9 - Commitments and Contingent Liabilities - Continued

Claims Handling Matters

Multidistrict Litigation

On September 2, 2003, the Judicial Panel on the Multidistrict Litigation entered an order transferring more than twenty putative class actions and derivative suits, described below, filed in various courts against the Company, several of its subsidiaries, and some of our officers, to the U.S. District Court for the Eastern District of Tennessee for coordinated or consolidated pretrial proceedings. The defendants strongly deny the allegations in each of these actions and will vigorously defend the substantive and procedural aspects of the litigations, except as noted below with respect to settlement discussions in the Plan Beneficiary Class Actions.

Shareholder Derivative Actions

On November 22, 2002, the first of five purported shareholder derivative actions was filed in the Tennessee Chancery Court. Between December 27, 2002 and March 11, 2003, four additional purported derivative actions were filed in state and federal courts in Tennessee. The defendants removed each of the actions that were filed in Tennessee state court to the U.S. District Court for the Eastern District of Tennessee.

Each of these actions purports to be brought on behalf of the Company against certain current and past members of our Board of Directors and certain executive officers alleging breaches of fiduciary duties and other violations of claims paying law by defendants. Plaintiffs allege, among other things, that the individual defendants breached their duties of good faith and loyalty by establishing or permitting to be established an unlawful policy of denying legitimate disability claims and improper financial reporting, and that certain defendants engaged in insider trading.

On October 17, 2003, the district court consolidated these actions under the caption In re UnumProvident Corporation Derivative Actions. On April 19, 2004, the plaintiffs filed a single consolidated amended complaint. On September 10, 2004, the defendants answered the consolidated amended complaint by denying generally the salient factual allegations in the complaint and by asserting various affirmative defenses.

Federal Securities Law Class Actions

On February 12, 2003, the first of six virtually identical putative securities class actions was filed in the United States District Court for the Eastern District of Tennessee. In two orders dated May 21, 2003, and January 22, 2004, the district court consolidated these actions under the caption In re UnumProvident Corp. Securities Litigation.

On January 9, 2004, the Lead Plaintiff filed its consolidated amended complaint on behalf of a putative class of purchasers of UnumProvident stock between March 30, 2000 and April 24, 2003. The amended complaint alleges, among other things, that we issued misleading financial statements, improperly accounted for certain impaired investments, failed to properly estimate our disability claim reserves, and pursued certain improper claims handling practices. The complaint asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5. On March 19, 2004, the defendants filed a motion to dismiss the consolidated amended complaint.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 9 - Commitments and Contingent Liabilities - Continued

On September 12, 2005, the court issued a Memorandum and Order denying in part, and granting in part, the motion to dismiss. The court granted the motion with respect to Lead Plaintiff s claims concerning our investments and denied the motion challenging the other alleged misstatements. Discovery, which had been stayed in this action pursuant to the Private Securities Litigation Reform Act of 1995, has now begun.

In May 2003, three identical putative securities class actions were filed in the Southern District of New York, which were later consolidated under the caption Azzolini v. CorTs Trust II for Provident Financial Trust, et al. A fourth action, Bernstein v. CorTs for Provident Financing Trust I, et al., was filed in the Eastern District of New York on July 7, 2003. These actions, which were transferred to Tennessee federal court, alleged claims on behalf of two different putative classes of purchasers of UnumProvident Corporate-Backed Trust Securities (CorTs) certificates that were issued by certain underwriter defendants unaffiliated with the Company. The amended complaints filed in each of these actions asserted claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 against UnumProvident and one of our officers. On September 16, 2005, the court issued a Memorandum and Order dismissing these actions with prejudice. On January 12, 2006, the Azzolini plaintiffs filed a notice of appeal from the court s decision dismissing this action. We reached an agreement with the Azzolini named plaintiffs settling all claims by those plaintiffs and providing for the withdrawal of their appeal. The amount of settlement was immaterial.

Policyholder Class Actions

On July 15, 2002, Rombeiro v. Unum Life Insurance Company of America, et al., was filed in the Superior Court of California and subsequently was removed to federal court, alleging that the plaintiff was wrongfully denied disability benefits under a group long-term disability plan. On January 21, 2003, an Amended Complaint was filed on behalf of a putative class of individuals that were denied or terminated from benefits under group long-term disability plans, seeking injunctive and declaratory relief and payment of benefits. On April 30, 2003, the court granted in part and denied in part the defendants motion to dismiss the complaint. On May 14, 2003, the plaintiff filed a Second Amended Complaint seeking similar relief.

Between November 2002 and November 2003, six additional similar putative class actions were filed in (or later removed to) federal district courts in Illinois, Massachusetts, New York, Pennsylvania, and Tennessee. The complaints alleged that the putative class members claims were evaluated improperly and allege that the Company and its insurance subsidiaries breached certain fiduciary duties owed to the class members under the Employee Retirement Income Security Act (ERISA), Racketeer Influenced Corrupt Organizations Act (RICO), and/or various state laws. The complaints sought various forms of equitable relief and money damages, including punitive damages.

These actions all were transferred to the Eastern District of Tennessee multidistrict litigation. On December 22, 2003, the Tennessee Federal District Court entered an order consolidating all of the above actions for all pretrial purposes under the caption In re UnumProvident Corp. ERISA Benefit Denial Actions and appointed a lead plaintiff. A consolidated amended complaint was filed on February 20, 2004. On March 26, 2004, the defendants answered the complaints and simultaneously filed a motion for judgment on the pleadings in the ERISA Benefit Denial Actions. The court has not yet ruled upon that motion.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

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Note 9 - Commitments and Contingent Liabilities - Continued

On April 30, 2003, a separate putative class action, Taylor v. UnumProvident Corporation, et al., was filed in the Tennessee Circuit Court and subsequently removed to federal court. The complaint alleges claims against UnumProvident and certain subsidiaries on behalf of a putative class of long-term disability insurance policyholders who did not obtain their coverage through employer sponsored plans and who had a claim denied, terminated, or suspended by a UnumProvident subsidiary after January 1, 1995, seeking equitable and monetary relief. Plaintiff alleges that the defendants violated various state laws by engaging in unfair claim practices and improperly denying claims.

On April 9, 2004, the plaintiffs in Taylor and in the ERISA Benefit Denial Actions separately filed motions seeking certification of a plaintiff class. On July 1, 2005, the defendants also filed motions for summary judgment in each action.

On December 14, 2005, the court granted in part the defendants motion for summary judgment in Taylor, dismissing plaintiff s request for equitable relief on her breach of contract claim and dismissing any claim plaintiff may make for punitive damages under the Tennessee Consumer Protection Act. The former claim is the principal claim upon which class certification is sought. The court reserved ruling on the remainder of the pending motion for summary judgment pending further mediation of the Taylor and ERISA Benefit actions.

Court ordered mediation has concluded with the settlement of all individual claims brought by six of the fifteen named plaintiffs in the ERISA Benefit Denial Actions. A seventh plaintiff has subsequently resolved her claims through the process established under the regulatory settlement agreements.

Plan Beneficiary Class Actions

On April 29, 2003, the first of two identical putative class actions, Gee v. UnumProvident Corporation, et al., was filed in the Eastern District of Tennessee on behalf of participants and beneficiaries of UnumProvident s 401(k) Retirement Plan (Plan), and the actions were later consolidated.

On January 9, 2004, plaintiffs filed a consolidated amended complaint against the Company, several of our officers and directors, and several alleged Plan fiduciaries on behalf of a putative class of individuals that held UnumProvident stock in their 401(k) retirement accounts subsequent to November 17, 1999. Plaintiffs allege that the defendants violated ERISA by making misrepresentations and omissions regarding investment in UnumProvident stock and by acting imprudently in failing to take action to protect participants from losses sustained from investments in the Plan s UnumProvident Stock Fund.

On February 26, 2004, the defendants filed a motion to dismiss contending that the complaint failed to state a valid claim under ERISA. On January 13, 2005, the court denied that motion. The defendants filed an answer to the complaint denying all material allegations on February 28, 2005.

On March 10, 2005, the plaintiffs filed a motion to certify the class. The defendants filed an opposition on June 10, 2005, and the matter is under submission with the court.

On November 30, 2005, the court entered a schedule providing for the completion of pretrial discovery by October 17, 2006. No trial date has been set for the action.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

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Note 9 - Commitments and Contingent Liabilities - Continued

The parties are currently engaged in settlement discussions supervised by a Court appointed mediator. The parties have reached an agreement in principle for resolution of the matter, the net cost of which is immaterial to the Company. The agreement is subject to further negotiations on a number of points, including attorneys fees, the preparation of a definitive written agreement, and Court approval of any final agreement.

Examinations and Investigations

The Company s U.S. insurance subsidiaries experienced increased market conduct examinations by state insurance departments during 2002 and 2003 focused specifically on our disability claims handling policies and practices. On March 19, 2003, we consented to the entry of an order by the Georgia Insurance Commissioner that, among other things, ordered four of the Company s U.S. insurance subsidiaries to each pay a monetary penalty of $250,000 and to adhere to certain claims handling practices. The order also placed these four companies on regulatory probation for two years. The Georgia order did not cite any violations of Georgia law or regulations.

The insurance commissioners of Maine, Massachusetts, and Tennessee initiated a multistate targeted market conduct examination in September 2003 that focused on the disability claims handling policies and practices of these subsidiaries. This multistate examination resulted in a report and regulatory settlement agreements that became effective on December 21, 2004, which was agreed to by 48 states and the District of Columbia. The examination report made no findings of violations of law or regulations. The examination identified areas of concern which became the focus of certain changes to our disability claims handling operations. The settlement agreements also include a reassessment of certain previously denied or closed claims, additional corporate and board governance, and payment of a fine in the amount of $15.0 million that was allocated among the states and jurisdictions participating in the agreements. The agreements will remain in place until the later of January 1, 2007, or the completion of an examination of claims handling practices and an examination of the reassessment process, both of which will be conducted by the lead state regulators. The settlement agreements also provide for a contingent fine of up to $145.0 million on the Company s U.S. insurance subsidiaries in the event that we fail to satisfactorily meet the performance standards in the settlement agreements relating to the examinations referred to above. The parties to the agreements have subsequently agreed to extend the reassessment process until December 31, 2007, and we expect to conclude the claim reassessment process by that time. The examinations will commence before or after that date. We believe that due to the changes we have made to our claims operations to enhance our oversight functions, it is not probable that we will fail to meet the performance standards in the agreements when these examinations are concluded.

In addition, the U.S. Department of Labor (DOL), which had been conducting an inquiry relating to certain ERISA plans, joined the settlement agreements. The Office of the New York Attorney General (NYAG), which had engaged in its own investigation of our claim handling practices, notified us that it supported the settlement and closed its investigation on this issue.

In the fourth quarter of 2004, we recorded a charge related to the settlement of the multistate market conduct examination of $127.0 million before tax, or $87.8 million after tax, comprised of four elements: $27.5 million of incremental direct operating expenses to conduct the two-year reassessment process; $44.0 million for benefit costs and reserves from claims reopened from the reassessment; $40.5 million for additional benefit costs and reserves for claims already incurred and currently in inventory that are anticipated as a result of the claim process changes being implemented; and the $15.0 million fine.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

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Note 9 - Commitments and Contingent Liabilities - Continued

On October 3, 2005, certain of the Company s U.S. insurance subsidiaries entered into a settlement agreement with the California Department of Insurance (DOI) in connection with a market conduct examination and investigation of the subsidiaries disability claims handling practices. The California DOI had chosen not to join the 2004 multistate settlement agreements.

As part of the settlement with the California DOI, we paid a civil penalty of $8.0 million and agreed to change certain practices and policy provisions related to our California business. The settlement also incorporates claims handling practices previously covered by the multistate settlement agreements and includes certain additional claim handling changes. Under the terms of the settlement, we will change certain provisions specific to California disability policies, and we received approval from the California DOI for the use of new individual and group disability policy forms. Following the California settlement, we also amended the multistate settlement agreements to include mailing a notice of eligibility to participate in the claim reassessment process to approximately 29,500 individuals whose claims were denied or terminated between January 1, 1997 and December 31, 1999. Under the original multistate settlement agreements, claimants during this period could request participation in the reassessment process, but they were not sent a notice.

In entering the settlement, we did not agree with the allegations and characterization of our past claims handling practices made by the California DOI.

Separately, we are proceeding with a plan to offer to reassess private label, acquired, and reinsured block claims, as well as claims administered on behalf of certain employers.

Based on the California DOI settlement agreement and related matters described above, in the third quarter of 2005 we recorded a charge of $75.0 million before tax, or $51.6 million after tax, comprised of four elements: $14.3 million of incremental direct operating expenses to conduct the reassessment process; $37.3 million for benefit costs and reserves from claims reopened from the reassessment; $15.4 million for additional benefit costs and reserves for claims already incurred and currently in inventory that are anticipated as a result of the claim process changes being implemented; and the $8.0 million fine.

Our quarterly review of our claim reassessment reserve adequacy includes an analysis of our assumptions related to:

1. the number of claimants who will ultimately choose to participate in the process,
2. the number of claimants for whom payments will be made and then closed because the claimant is no longer disabled,
3. the number of claimants for whom payments will continue because the claimant remains eligible for disability payments, and
4. the average incurred cost per claimant.

When we performed our analysis at the end of the first quarter of 2006, our analysis was based on data available as of the end of that time period. At that time we believed that the actual results were credible enough to enable us to update our estimate of the ultimate cost related to the reassessment process and the reserves established at the time of the settlement agreements. At the end of the first quarter, we concluded that a change in our initial assumptions was warranted. The change in assumptions was primarily related to the number of claimants for whom payments will continue because the claimant remains eligible for disability payments. We therefore recorded a charge, in the first quarter of

2006, of $86.0 million before tax, or $55.9 million after tax, to reflect our then current best estimate of the ultimate cost of benefits for claims reopened in the reassessment process. When we recorded this charge, we

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Note 9 - Commitments and Contingent Liabilities - Continued

based our estimate on the information that existed at that time, which was the actual cost related to approximately 20 percent of the projected ultimate total of 25,000 claims expected to be reassessed. The characteristics, profile, and cost of those initial 20 percent of claims were more statistically credible than the information on which we based the initial charges in 2004 and 2005.

In the third quarter of 2006, we began to experience increasingly higher monthly benefit costs related to the claim reassessment process. In analyzing the reason for this increase, our experience for two of the major assumptions used to calculate the reserves had exceeded our expectations. Those two assumptions were: (1) the number of decisions being overturned by the reassessment process, and (2) the average cost per reassessed claim.

The following provides additional information that will highlight the shift in assumptions:

1. From the inception of the reassessment process in January 2005 through March 2006, approximately 23 percent of the decisions made when the claim was originally submitted were overturned in the reassessment.

2. From April through September 2006, the overturn rate averaged 50 percent, with the most dramatic shift occurring in the third quarter.

3. This recent change increased the average overturn rate from 23 percent experienced through March 2006 to 36 percent at September 2006 from inception to date.

4. This shift appears to be due to a higher than expected level of claimants whose disability deteriorated since the initial claim decision and/or whose disability has now qualified the claimant to receive Social Security benefits.

5. The average incurred cost during the period April through September 2006 was also slightly higher than the average cost associated with the period from inception through March 2006.

6. Our assumption concerning the total number of claims projected to be reassessed is still generally consistent with the levels originally assumed.

Based on these changes, in the third quarter of 2006 we increased our estimate for the total cost of this reassessment process by $325.4 million before tax, or $211.5 million after tax. The third quarter charge was comprised of $310.4 million to reflect our revised estimate of future obligations for benefit costs for claims reopened in the reassessment and $15.0 million for additional incremental direct claim reassessment operating expenses because of the additional time now estimated to complete the process. Our third quarter of 2006 provision for the cost of this process was based on the cost of approximately 55 percent of the projected ultimate total of 25,000 claims expected to be reassessed. Our best estimate of $310.4 million for the reopened claims assumes that the nature and characteristics of the approximately 45 percent remaining claims estimated to be reassessed in the future are similar to the average profile of the 55 percent already reviewed.

If, however, the estimated 45 percent of remaining claims have a profile more reflective of the most recent monthly experience, we believe our costs could be higher by approximately $90.0 million. If the remaining claims have a profile more reflective of our earlier experience, we believe our costs could be lower by approximately $90.0 million. The estimate of the lower and upper end of the range of reasonably possible additional costs is much less certain than the best estimate upon which our accruals are currently based and uses assumptions, among the range of reasonably possible outcomes, which are more favorable to us at the lower end of the cost range and less favorable to us at the upper end of the range.

We will continue to monitor our claim reassessment experience and review the adequacy of the associated reserves on a quarterly basis. Unfavorable experience relative to our revised assumptions could result in additional claim reassessment costs above our current accrual and within or in excess of our reasonably possible range.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 9 - Commitments and Contingent Liabilities - Continued

On March 29, 2006 the Company received a subpoena from the Securities and Exchange Commission (SEC) seeking information regarding certain reinsurance transactions and transactions regarding Non Traditional Products entered into after January 1, 2002. We are cooperating fully with the SEC in its investigation.

These and other regulatory examinations or investigations could result in, among other things, changes in business practices, including changes in broker compensation and related disclosure practices, changes in the use and oversight of finite reinsurance, changes in governance and other oversight procedures, fines, and other administrative action.

Such results, singly or in combination, could injure the Company s reputation, cause negative publicity, adversely affect our debt and financial strength ratings, or impair our ability to sell or retain insurance policies, thereby adversely affecting our business, and potentially materially adversely affecting the consolidated results of operations in a period, depending on the results of operations for the particular period. Determination by regulatory authorities that the Company or its insurance subsidiaries have engaged in improper conduct could also adversely affect our defense of various lawsuits described herein.

Other Claim Litigation

The Company and its insurance company subsidiaries, as part of our normal operations in managing disability claims, are engaged in claim litigation where disputes arise as a result of a denial or termination of benefits. Most typically those lawsuits are filed on behalf of a single claimant or policyholder, and in some of these individual actions punitive damages are sought, such as claims alleging bad faith in the handling of insurance claims. For our general claim litigation, we maintain reserves based on experience to satisfy judgments and settlements in the normal course. We expect that the ultimate liability, if any, with respect to general claim litigation, after consideration of the reserves maintained, will not be material to our consolidated financial condition. Nevertheless, given the inherent unpredictability of litigation, it is possible that an adverse outcome in certain claim litigation involving punitive damages could, from time to time, have a material adverse effect on our consolidated results of operations in a period, depending on the results of operations for the particular period. We are unable to estimate a range of reasonably possible punitive losses.

On December 20, 2004, Weiller v. New York Life Insurance Company, et al., was filed in New York Supreme Court against, among others, UnumProvident and certain subsidiaries on behalf of a putative class of insureds under policies issued by several third-party insurers on behalf of whom UnumProvident administers claims. The complaint alleges that the defendants breached the insurance policies by improperly denying or terminating benefits, and seeks equitable relief on behalf of the class and benefits on behalf of the named plaintiff. We denied the allegations and vigorously defended against the allegations raised in the complaint. On February 18, 2005, the defendants filed a motion to dismiss this action. On June 20, 2005, the plaintiff filed a motion seeking certification of a putative class, which the defendants opposed. On April 27, 2006, the court denied class certification and dismissed all claims except the individual contract claim of plaintiff. Plaintiff has appealed these orders. The parties have reached a settlement of the case while this appeal was pending. Under the terms of the settlement, the plaintiff will release all claims and withdraw his appeal. The amount of settlement was immaterial.

From time to time class action allegations are pursued, as in Weiller, where the claimant or policyholder purports to represent a larger number of individuals who are similarly situated. Since each insurance claim is evaluated based on its own merits, there is rarely a single act or series of actions, which can properly be addressed by a class action. Nevertheless, we monitor these cases closely and defend the Company appropriately where these allegations are made.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 9 - Commitments and Contingent Liabilities - Continued

Broker Compensation, Quoting Process, and Related Matters

Examinations and Investigations

In June 2004, the Company received a subpoena from the NYAG requesting documents and information relating to compensation arrangements between insurance brokers or intermediaries and the Company and its subsidiaries. The Company has received additional subpoenas or requests for additional information from the NYAG concerning its relations with insurance brokers. The NYAG has filed several lawsuits against brokers arising out of its investigation. Several insurers were cited in the complaints but not named as defendants; one such complaint cited the Company but did not name it as a defendant. We are cooperating fully with the NYAG s investigations and inquiries.

Since October 2004, the Company and/or its insurance subsidiaries have received subpoenas or information requests from the NYAG, a Federal Grand Jury in San Diego, the District Attorney for the County of San Diego, insurance departments, and/or other state regulatory or investigatory agencies of at least eight additional states including Connecticut, Florida, Maine, Massachusetts, North Carolina, Oklahoma, South Carolina, and Tennessee.

The subpoenas and information requests sought information regarding, among other things, quoting processes, producer compensation, solicitation activities, policies sold to state or municipal entities, and information regarding compensation arrangements with brokers, particularly with regard to Universal Life Resources, Inc. We have cooperated fully with these investigations.

On November 1, 2006, the Company entered into a settlement agreement with the NYAG in the form of an assurance of discontinuance that provides for a national restitution fund of $15.5 million and a fine of $1.9 million, the costs of which were recorded in the third quarter of 2006. Under the settlement agreement, we will be implementing a new, simpler compensation program for our group products. Additionally, we are expanding our disclosure of broker compensation programs. We had previously established, in March 2005, disclosure policies that provided customers with a means of obtaining information about the compensation paid to their brokers. We at that time discontinued all programs that provided loans, equity investments, contests, and trips.

In addition to this settlement, we have been previously informed by the Oklahoma Department of Insurance that its investigation was closed without finding. With respect to the other states listed, other than Florida and other than those with whom settlements have been reached, we have not received any further inquiries in the past 12 months and consider those investigations to be dormant.

We have also had discussions with the DOL regarding compliance with ERISA, relating to our interactions with insurance brokers and to regulations concerning insurance information provided by us to plan administrators of ERISA plans, including specifically the reporting of fees and commissions paid to agents, brokers, and others in accordance with the requirements of Schedule A of Form 5500. The DOL is pursuing an investigation of the Company concerning these issues, both generally and specifically in connection with certain brokers, including Universal Life Resources, Inc. We are cooperating fully with the DOL s investigation.

Broker-Related Litigation

The Company and certain of its subsidiaries, along with many other insurance brokers and insurers, have been named as defendants in a series of putative class actions that have been transferred to the U.S. District Court for the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 9 - Commitments and Contingent Liabilities - Continued

District of New Jersey for coordinated or consolidated pre-trial proceedings as part of multidistrict litigation (MDL) No. 1663, In re Insurance Brokerage Antitrust Litigation. The plaintiffs in MDL No. 1663 filed a consolidated amended complaint in August 2005, which alleges, among other things, that the defendants violated federal and state antitrust laws, RICO, ERISA, and various state common law requirements by engaging in alleged bid rigging and customer allocation and by paying undisclosed compensation to insurance brokers to steer business to defendant insurers. Defendants filed a motion to dismiss the complaint on November 29, 2005. Oral argument on the motion to dismiss was held on July 26, 2006. On October 3, 2006 the Court ordered plaintiffs to replead their Sherman Act and RICO claims with particularity by October 25, 2006 and scheduled a status conference for November 6, 2006 for defendants to advise the Court whether they plan to submit additional briefing on the motion to dismiss and/or to move for summary judgment. The Court denied defendants motion to dismiss the ERISA claims, while setting an expedited schedule for completion of discovery and noting that these claims were more appropriately addressed on summary judgment. Finally, the Court held in abeyance the motion to dismiss the state law claims pending final resolution of the motions to dismiss the federal claims.

Plaintiffs filed a motion for class certification on February 13, 2006, and defendants filed an opposition. The motion for class certification is fully briefed and pending. The class certification hearing is currently scheduled for January 9, 2007.

The Company was a defendant in a case brought by the California Insurance Commissioner, styled California v. Universal Life Resources, et al., filed in California Superior Court. The Complaint sought only to impose injunctive relief under the California Insurance Code based on allegations of undisclosed or inadequately disclosed compensation paid to brokers, steering, bid rigging, and customer allocation similar to the claims asserted in MDL No. 1663. The defendants filed a demurrer to the Second Amended Complaint on July 21, 2005. The demurrer was overruled on December 23, 2005, and we filed an answer denying all material allegations on January 18, 2006. On November 1, 2006, the Company resolved its litigation with the California Insurance Commissioner by agreeing to implement a series of new disclosure practices related to producer compensation that are similar to those agreed to with the NYAG, as disclosed above. As part of that agreement, the Company has agreed to pay the reasonable attorneys fees incurred by the California DOI in this litigation, the cost of which was recorded in the third quarter of 2006.

The Company is a defendant in an action styled, Palm Tree Computers Systems, Inc. v. ACE USA, et al., which was filed in the Florida state Circuit Court on February 16, 2005. The complaint is a putative class action and alleges violations of the Deceptive and Unfair Trade Practices Act of Florida and other states, breach of fiduciary duty, and unjust enrichment. The allegations are brought against numerous broker organizations and insurers and assert the Company and its subsidiaries engaged in illegal and unethical contingent commission arrangements. The case was removed to federal court and, on October 20, 2005, the case was transferred to the District of New Jersey multidistrict litigation. A motion to remand the case to the state court in Florida remains pending, but no further action has been taken in the case subsequent to the transfer.

On December 21, 2004, a putative derivative action styled Leonard v. UnumProvident Corporation, et al., was filed in Tennessee Chancery Court against the Company and various members of our board of directors alleging claims on behalf of the Company against the director defendants for breach of duty, mismanagement, and corporate waste, challenging certain compensation paid to insurance brokers and alleging insider trading against certain director defendants. On April 1, 2005, the defendants moved to dismiss the complaint on the grounds that the plaintiff failed to make a pre-suit demand on our board of directors and that the complaint fails to state a claim upon which relief could be granted. That motion remains pending. The defendants strongly deny the allegations in the complaint and will vigorously defend both the substantive and procedural aspects of the litigation.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 9 - Commitments and Contingent Liabilities - Continued

We deny the allegations in these matters and intend to vigorously contest them, except as previously noted with respect to the action brought by the California Insurance Commissioner.

Miscellaneous Matters

In September 2003, United States of America ex. rel. Patrick J. Loughren v. UnumProvident Corporation and GENEX Services, Inc., was filed in the United States District Court for the District of Massachusetts. This is a qui tam action to recover damages and civil penalties on behalf of the United States of America alleging violations of the False Claims Act by the Company and its GENEX Services, Inc. (GENEX) subsidiary. In accordance with the False Claims Act, the action was originally filed under seal to provide the government the opportunity to investigate the allegations and prosecute the action if they believed that the case had merit and warranted their attention. The government declined to prosecute the case and the case became a matter of public record on December 23, 2004. The complaint alleges that the Company defrauds the government by inducing and or assisting disability claimants to apply for disability benefits from the Social Security Administration (SSA) when the Company allegedly knows that the claimants are not disabled under SSA criteria. On September 13, 2005, the magistrate judge filed a recommended decision granting the Company s motion to dismiss. The plaintiffs appealed that finding to the district court judge. On October 6, 2005, the district court judge adopted, in full, the recommended decision of the magistrate judge thereby granting dismissal of the case. The plaintiffs subsequently amended their pleading, and the Company filed a motion to dismiss the pleading as amended for the same reasons that the court dismissed the original pleading. On February 9, 2006, the Court denied the motion to dismiss. We intend to vigorously defend the action.

In certain of our reinsurance businesses there are disputes among the pool members, reinsurance participants, and/or reinsurers concerning the scope of their obligations and liabilities within the reinsurance contracts, including the reinsurance pools for which subsidiaries of the Company acted either as pool managers or underwriting agents, as pool members, or as reinsurers. The Company or the Company s subsidiaries either have been or may in the future be brought into disputes, arbitration proceedings, or litigation with other pool members or reinsurers in the process of resolving the various claims.

Various other lawsuits against the Company have arisen in the normal course of its business. Contingent liabilities that might arise from such other litigation incurred in the normal course of business are not deemed likely to materially adversely affect the consolidated financial position or results of operations in a period, depending on the results of operations for the particular period.

Note 10 - Reinsurance

During the third quarter of 2005, we recaptured a closed block of individual income protection business originally ceded to Centre Life Reinsurance Ltd. in 1996. The recaptured business includes approximately $1.6 billion in invested assets and $185.0 million of annual premium. The effective date of the recapture was August 8, 2005. The underlying operating results of the reinsurance contract, prior to recapture, were reflected in other income. The recapture therefore did not have a material impact on operating income for the Individual Income Protection Closed Block segment.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued

UnumProvident Corporation and Subsidiaries

September 30, 2006

Note 11 - Acquisitions and Dispositions

During the third quarter of 2005, our wholly-owned subsidiary, Unum Limited, completed the sale of its Netherlands branch. The gain on the sale was approximately $5.7 million before tax and $4.0 million after tax and is included in operating results for the three and nine month periods ended September 30, 2005.

During the third quarter of 2005, our wholly-owned subsidiary, GENEX Services, Inc. (GENEX), acquired Independent Review Services, Inc., a provider of medical diagnostic networks and independent medical examinations, at a price of $3.5 million.

Note 12 - Income Tax

During the first quarter of 2005, the Internal Revenue Service completed its examination of tax years 1999 through 2001 and issued its revenue agent s report (RAR) in April 2005. Income tax liabilities of approximately $32.0 million that related primarily to interest on the timing of expense deductions were released in the first quarter of 2005, all of which was reflected as a reduction to income tax expense.

In the third quarter of 2005, we recognized an income tax benefit of approximately $10.8 million related to the finalization of income tax reviews of our U.K. subsidiaries.

Note 13 - Subsequent Event

On November 1, 2006, Tailwind Holdings, LLC (Tailwind Holdings), a newly formed Delaware limited liability company and a wholly-owned subsidiary of UnumProvident, issued $130.0 million of senior, secured notes in a private placement. Recourse for the payment of principal, interest, and other amounts due on the notes will be dependent principally on the receipt of dividends from Tailwind Reinsurance Company (Tailwind Re), the sole subsidiary of Tailwind Holdings. The ability of Tailwind Re to pay dividends to Tailwind Holdings will depend on its satisfaction of applicable regulatory requirements and on the performance of the reinsured claims of Unum Life Insurance Company of America (Unum America) reinsured by Tailwind Re. None of UnumProvident, Unum America, Tailwind Re, or any other affiliate of Tailwind Holdings is an obligor or guarantor on the notes.

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Report of Ernst & Young LLP, Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

UnumProvident Corporation

We have reviewed the consolidated statement of financial condition of UnumProvident Corporation and subsidiaries as of September 30, 2006, and the related consolidated statements of operations for the three-month and nine-month periods ended September 30, 2006 and 2005, and the consolidated statements of stockholders equity and cash flows for the nine-month periods ended September 30, 2006 and 2005. These 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, 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 the standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of financial condition of UnumProvident Corporation and subsidiaries as of December 31, 2005, and the related consolidated statements of operations, stockholders equity, and cash flows for the year then ended not presented herein, and in our report dated February 28, 2006, we expressed an unqualified opinion on those consolidated financial statements.

/s/ ERNST & YOUNG LLP

Chattanooga, Tennessee

November 1, 2006

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

UnumProvident Corporation, which we refer to as UnumProvident, and its insurance and non-insurance companies, which collectively with UnumProvident we refer to as the Company, operate in the United States, the United Kingdom, and, to a limited extent, in certain other countries around the world. The principal operating subsidiaries in the United States are Unum Life Insurance Company of America, Provident Life and Accident Insurance Company, The Paul Revere Life Insurance Company, and Colonial Life & Accident Insurance Company, and in the United Kingdom, Unum Limited. We are the largest provider of group and individual income protection insurance products in the United States and the United Kingdom. We also provide a complementary portfolio of other insurance products, including long-term care insurance, life insurance, employer- and employee-paid group benefits, and other related services.

We have three major business segments: U.S. Brokerage, Unum Limited, and Colonial, as well as the Individual Income Protection Closed Block segment, Other segment, and Corporate segment. These segments are discussed more fully under Segment Operating Results included in this Form 10-Q.

We offer a comprehensive portfolio of income protection products and services to meet the diverse needs of the marketplace. We seek to achieve a competitive advantage by offering group, individual, and voluntary workplace products that can be offered as stand alone products or that can be combined with other coverages to provide integrated and individualized product solutions for customers. We offer businesses of all sizes competitive benefit plans to protect the incomes and lifestyles of employees and their families. Through a variety of technological tools and trained professionals, we offer services, including comprehensive claims management services, which are designed to meet the evolving needs of our customers. We strive to be responsive and timely, and we are committed to service excellence.

We believe that we are a well positioned and competitive force in our sector. However, due to the nature of our business, we are sensitive to economic and financial market movements, including consumer confidence, employment levels, and the level of interest rates.

The discussion and analysis presented in this section should be read in conjunction with the consolidated financial statements and notes thereto in Part I, Item 1 contained in this Form 10-Q and with the discussion, analysis, and consolidated financial statements and notes thereto in Part I, Items 1 and 1A, and Part II, Items 6, 7, 7A, and 8 of our annual report on Form 10-K for the year ended December 31, 2005.

Executive Summary

In commenting on our results for the third quarter of 2006, we will discuss four major topics: operating performance of our three major business segments, our closed block of individual income protection business, our outstanding legal and regulatory issues, and our capital management initiatives. Although we reported a net loss for the third quarter of 2006 because of the revision in our estimate for the cost of the claim reassessment process, we had excellent underlying operating performance in several of our lines of business and improved performance in many of the other lines of business, moved forward on or settled several regulatory and legal matters, and continued to make progress toward our capital management objectives. Concerning the revision of our claim reassessment reserve, we were able to increase the reserve with only minor disruption to our holding company cash position, our regulatory risk-based capital ratios, and our corporate leverage ratios.

Operating Performance of our Major Business Segments

For the third quarter of 2006 we reported solid operating results in all of our U.S. Brokerage segment lines of business, with our supplemental and voluntary lines reporting improved results relative to both the prior year and the previous quarters of 2006. Group life and accidental death and dismemberment lines of business reported consistent results year over year. Although our U.S. Brokerage group long-term income protection line of business is not yet performing at the level of our long-term expectations due to claims management performance, we are pleased with the progress made during 2006 in improving the profitability in this line of business. We believe we have taken the necessary actions to improve claim operational effectiveness over the long term and have experienced improvements in the area of claims management performance during 2006, with greater consistency in claim recovery rates and in the timing of claim decisions. We expect additional improvements to occur during the remainder of 2006 and into 2007. Positive trends continue to emerge for our U.S. Brokerage group long-term income protection line of business, including: favorable pricing trends; stable to declining claim incidence trends; renewal profit improvement; aggressive management of expenses; improvements in operating effectiveness; and the management of persistency of the in-force block of business, which includes retaining business that is more profitable than business which terminates. Separate and distinct from our current operational trends is the third quarter of 2006 revision of our claim reassessment reserve, discussed more fully below, which reflects our commitment to comply fully with our regulatory settlement agreements.

Third quarter of 2006 sales for U.S. Brokerage decreased relative to last year s third quarter, with the decline driven primarily by a decrease in our average case size for our group markets and overall lower industry sales in group income protection. On a year-to-date basis, sales increased slightly compared to the prior year, with sales in our group core market segment increasing and sales in the group large employer market decreasing. These year-to-date results are reflective of our mix of business focus, as we continue our efforts to increase the portion that our group core market segments contribute to our overall U.S. Brokerage business mix. We reported sales growth in our U.S. Brokerage voluntary workplace benefits line of business for both the third quarter and first nine months of 2006 relative to the prior year periods.

Our Unum Limited segment continues to produce excellent operating results, with an increase in third quarter segment operating income of 31.5 percent compared to the third quarter of 2005. Sales in Unum Limited, which have been challenging throughout 2006, improved in the third quarter relative to the first two quarters of 2006. Sales in this market have been negatively impacted during 2006 by lower activity caused by distraction in the U.K. employee benefits market due to changes in pension legislation. However, U.K. legislative changes that remove discrimination by employers on the basis of age, therefore requiring the extension of insurance coverage, became effective in October 2006. As a result, we anticipate that Unum Limited sales will increase from current levels towards the end of the year and into 2007. We expect to maintain our significant market position in the highly competitive U.K. market.

Our Colonial segment also had excellent operating results in the third quarter of 2006, with an increase in segment operating income of 24.0 percent compared to the prior year third quarter. Colonial reported considerable sales growth in the third quarter and first nine months of 2006 compared to last year. Sales in the large case market, which is comprised of employee groups with 2,000 lives or greater, increased significantly in 2006 relative to the prior year periods, partially due to the sale of two large accounts during the third quarter of 2006. Sales in the core markets, which are comprised of employee groups with less than 2,000 lives, also increased in the third quarter and first nine months relative to the prior year periods. We continue to focus on profitable and sustainable sales growth for this segment.

During 2006, we have continued to diversify and improve our business balance by growing Unum Limited, Colonial, and our U.S. Brokerage supplemental and voluntary product lines and by shifting our U.S. Brokerage group lines of business into a more balanced mix between small and mid-employer core market segments and the large employer market segment. While facing challenging market conditions, we have remained focused on maintaining our disciplined approach to pricing and underwriting. Although we have shifted our mix of group business, we continue to lead the U.S. disability income protection insurance marketplace, according to the 2005 JHA group and individual disability market survey results announced during the second quarter of 2006. As measured by inforce premium, we hold a 22.5 percent share in the U.S. group disability market and a 36 percent share in the U.S. individual disability market. It is the 30th consecutive year that we have led the U.S. group disability income protection industry. In the U.K. market, according to the GEIS 2006 survey which is based on inforce premium, we have maintained our significant market position, with approximately 56.9 percent of the U.K. group disability market. We believe that our continued leadership position is a testament to both the quality of our products and services as well as the strong relationships we have established over the years with both our customers and brokers. We believe, and independent market surveys indicate, that we have been successful in maintaining a solid reputation and strong relationships with our customers and producers. Survey ratings for our products and

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services remain favorable, and ratings for our image and reputation are also favorable, showing improvement over prior periods.

We constantly look for opportunities to improve the consistency of business plan execution, and to this end we have initiated actions to do so. We have improved technology solutions in our administration areas and implemented a focused plan for consistent service delivery in our customer service areas. We have completed the first phase of a customer-oriented business model which not only provides products and services that meet the needs of the marketplace but is also supported by front-to-back business processes and technology. We have also introduced a new web-based enrollment platform for our workplace benefits products that will help employees fully understand the benefit coverage provided by an employer and the additional insurance options that may be available at the workplace. We have joined with Matria Healthcare to create a new disability and disease management partnership aimed at helping employers combat rising healthcare costs and improve workforce productivity.

As an active component of our day to day activities, we manage the credit risk and interest rate risk in our investment portfolio. During the first nine months of 2006, the relationship between our reserve discount rates and the respective portfolio yield rates remained within our target ranges, despite the third quarter decline in interest rates. We work to match the cash flows of our investment portfolios with the cash flows of our liabilities to eliminate as much as possible our exposure to changes in the overall level of interest rates. While our core investments are investment grade corporate fixed maturity securities, we also invest in other asset categories for diversification and yield. Our investment portfolio is well diversified across industry sectors and geographically diversified with respect to our mortgage loan portfolio. The average quality of our fixed maturity security portfolio was A2 at the end of the third quarter of 2006.

We believe that the actions we have taken during the past several years, as well as the plans we are executing in 2006, will improve the effectiveness of the basic functions of our businesses, reduce our business volatility, and lead to a greater consistency in the execution of our business plan.

Individual Income Protection Closed Block Segment

We continue to examine strategies to improve the capital efficiency of our closed block of individual income protection business. Because we cannot reprice this closed block of business, our focus has been on how we can more effectively manage the capital supporting this business. Our three major operating segments are supported by approximately $6.4 billion of allocated capital and produce a return on equity that is generally consistent with our current plan and on target to attain our long-term goal for return on equity. The closed block of individual income protection is supported by approximately $2.6 billion of allocated capital, and our return on equity for this business generally is in the low single digits. With the successful completion of the securitization of a small block of our group long-term income protection claim reserves on November 1, 2006, we are cautiously optimistic that we can complete a similar transaction for our closed block of individual income protection claim reserves. We believe that a transaction of this nature would allow us to divert some of the capital currently supporting this block of business to support other initiatives and therefore increase our total consolidated return on equity.

Legal and Regulatory Issues

During the third quarter of 2006, we made progress in settling some of our outstanding legal and regulatory issues as described in Note 9 of the Notes to Consolidated Financial Statements contained in Item 1. We recently reached an agreement in principle with the plaintiffs (subject to court approval) on the plan beneficiary class action, or 401(k) case, which is one of the multidistrict litigation matters outlined in our litigation footnote.

In addition, we also recently announced that we had reached a settlement agreement on broker compensation with the Office of the New York Attorney General (NYAG) that directly resolves all issues raised by the NYAG in its review of our broker compensation practices. The review was part of a larger investigation of broker compensation practices in the insurance industry. We also resolved litigation filed by the California Insurance Commissioner against our Company and other insurers regarding disclosure practices in broker compensation. Under the settlements, we will be implementing a new, simpler compensation program for our group products. Additionally, we are expanding our disclosure of broker compensation programs, enhancing a policy that we believe is already among the most comprehensive in the industry. We had previously taken a number of steps which we believe enhanced transparency by establishing, in March 2005, disclosure policies that provided customers with a means of obtaining information about the compensation paid to their brokers. We at that time discontinued all programs that provided loans, equity investments, contests, and trips. As part of the settlement with the NYAG, we agreed to pay a fine of $1.9 million and to establish a fund of $15.5 million to provide restitution for any customer determined to be harmed by past practices. These charges were recorded in the third quarter of 2006.

We believe that we removed substantial regulatory uncertainty surrounding our claims practices through the settlement agreement with the California Department of Insurance (DOI) in 2005 and the settlement of the multistate market conduct examinations in 2004 and continue to focus a great deal of resources on meeting the requirements of these agreements. We meet periodically with regulators and maintain an ongoing dialogue with them to communicate the progress we are making. Additionally, we routinely engage in discussions related to other issues which could impact any of our companies.

The revision of our claim reassessment reserve in the first and third quarters of 2006, discussed in the following section, reflects our continued commitment to comply fully with our regulatory settlement agreements. This is an unprecedented process, and thus the cost has been difficult to estimate. Because we are basing our revised third quarter estimate on approximately 55 percent of the ultimate number of decisions rather than approximately 20 percent of the ultimate number, as was necessary in the first quarter, we believe that the data upon which it is based is more statistically credible. The reassessment process is completely separate from our ongoing claim operation and will be concluded by the end of 2007. Based on the 55 percent of claims already reviewed and our estimate for the remaining 45 percent of claims to be reassessed, both the number of claim decisions overturned and the associated claim payments on the reopened claims equal approximately two percent of the total group and individual long-term income protection claim decisions and claim payments made during the time period covered by the reassessment process.

We have completed the mailing of virtually all of the required claim reassessment notices. Those individuals who want their claims reviewed have the opportunity to request a claim reassessment information form and have 60 days to complete the form once it is received. Through mid-October 2006, approximately 27 percent of the recipients of the reassessment notice have requested claim reassessment information forms. Claim reassessment information forms have been sent to approximately 73 percent of those requesting the form, and of those sent out, 26 percent have been returned. We expect that the rate of response for reassessment will increase over time as many of the individuals have unexpired time remaining to request and complete the necessary information forms.

A more thorough discussion of these issues, as well as an update of our other outstanding legal and regulatory issues, is included in the following section First Nine Months 2006 Significant Transactions and Events and in Note 9 of the Notes to Consolidated Financial Statements contained in Item 1.

Capital Management Initiatives

Our significant capital management accomplishments during 2005 established a foundation for improved financial flexibility in 2006 and beyond. The risk-based capital ratio for our U.S. insurance subsidiaries, calculated on a weighted average basis using the National Association of Insurance Commissioners Company Action Level formula, was above 300 percent at the end of 2005.

In November 2005, we repatriated $454.8 million in unremitted foreign earnings under the Homeland Investment Act of 2004. In 2005 we repaid $227.0 million of maturing debt, completed a long-term debt offering in conjunction with the November repatriation, and in the first quarter of 2006 purchased and subsequently retired $400.0 million of the senior note element of our remarketed adjustable conversion-rate equity security units issued during 2003. In May 2006, upon settlement of the common stock purchase contract of the adjustable conversion-rate equity security units, we received approximately $575.0 million and issued 43.3 million shares of common stock. We continued to lower our debt through the purchase of $300.0 million of tendered debt and capital securities in the second quarter of 2006. With these actions, we have reduced our financing risk by lowering our consolidated debt and smoothing our debt maturity schedule. Further, during 2006 we have made voluntary contributions of $92.0 million to our U.S. qualified defined benefit plan and $44.2 million to our U.K. defined benefit plan.

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We continue to execute our capital management initiatives to further build on our foundation of improved financial flexibility, and on November 1, 2006, we announced the completion of our securitization of approximately $1.5 billion of group long-term income protection claim reserves through the issuance of $130.0 million senior, secured notes of our wholly-owned subsidiary Tailwind Holdings, LLC (Tailwind Holdings). This offering increases our financial flexibility as we continue to implement long-term capital management strategies that are aligned with our capital management initiatives.

The additional costs related to the claim reassessment process contributed to a lower combined statutory capital and surplus for our U.S. insurance subsidiaries, which was approximately $4.036 billion at September 30, 2006, compared to $4.270 billion at December 31, 2005. We have revised our capital plan and believe that our combined risk-based capital ratio for our U.S. insurance subsidiaries will be at or near our target level at year end 2006.

Our capital planning objectives continue to be: maintain our risk-based capital ratio at approximately its current level; maintain our leverage ratio at current levels while exploring the potential benefits of further reductions; maintain holding company liquidity to cover at least six months of debt interest service in addition to an amount equal to the after tax cost of t