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# ING U.S., Inc. (VOYA)

Q3 2013 Earnings Call


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# MANAGEMENT DISCUSSION SECTION

**Operator**: Good morning, and welcome to the ING U.S. Third Quarter 2013 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] Participants are limited to one question and one follow-up. Please note this event is being recorded.

I would now like to turn the conference over to Darin Arita, Senior Vice President Investor Relations. Please go ahead.

## Darin Arita
*Senior Vice President, Investor Relations, ING U.S., Inc.*

Thank you, Emily, and good morning, everyone. Welcome to ING U.S.'s third quarter 2013 conference call. A slide presentation for this call is available on our website at investors.ing.us or via the webcast.

Turning to slide two, on today's call, we will be making forward-looking statements. Except with respect to historical information, statements made in this conference call constitute forward-looking statements within the meaning of federal securities laws, including statements relating to trends in the company's operations and financial results and the business and the products of the company and its subsidiaries.

ING U.S.'s actual results may differ materially from the results anticipated in the forward-looking statements as a result of risks and uncertainties including those from time-to-time in ING U.S.'s filings with the U.S. Securities and Exchange Commission.


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ING U.S. specifically disclaims any obligation to update or revise any forward-looking statements whether as a result of new information, future developments or otherwise.

Slide two also notes that the call today includes non-GAAP financial measures. An explanation of how we calculate these measures and the reasons we believe they're useful, can be found in the quarterly investor supplement available on our website at investors.ing.us.

Reconciliations to the most directly comparable GAAP measures are included in the press release and the quarterly investor supplement.

Joining me this morning on the call are, Rod Martin, Chairman and Chief Executive Officer of ING U.S.; Alain Karaoglan, Chief Operating Officer and Ewout Steenbergen, Chief Financial Officer. After their prepared remarks, we will take your questions.

With that, let's turn to slide three and I will turn the call over to Rod.

## Rodney O. Martin

*Chairman & Chief Executive Officer, ING U.S., Inc.*

Thank you, Darin, and good morning. Following our first six months as a public company, we're pleased with the steady progress we're making. Our progress is being driven by a combination of solid execution and firm financial discipline, key elements of our transformation story. Our financial results for the first nine months of 2013 are on track with our plan and reflect our commitment to helping customers with their retirement readiness.

In addition to our solid financial performance over the past quarter, we also achieved key strategic results that amplify the progress we're making. First, we completed our recapitalization plan in July. Second, we launched our first phase of our rebranding to Voya Financial. Investment Management is leading the way and will become Voya Investment Management on May 1, 2014.

Third, we've recently concluded a roadshow in connection with ING Group's offering of approximately 38 million shares of our common stock. In addition to attracting new investors and selling more shares to existing shareholders, ING Group was able to reduce their ownership stake to approximately 57%.

These accomplishments are all important validations of our ability to effectively execute key elements of our transformation strategy while at the same time delivering solid financial results. We're confident in our ability to execute on our long-term plan.

As we move to slide four, let me highlight a few financial measures from the third quarter. We achieved total after-tax operating earnings of $238 million or $1.08 per diluted share. While this assumes a tax rate of 35%, our actual tax rate for the quarter was close to zero.

We also generated net income available to common shareholders of $347 million. The net income result in the third quarter was driven by solid operating earnings from our Retirement Solutions, Investment Management, and Insurance Solutions businesses, favorable DAC unlocking related to the annual actuarial review of assumptions, which Ewout will cover in more detail, and the benefit of net partnership income during the quarter.

The measure we used to calculate ROE in our Retirement Solutions, Investment Management, and Insurance Solutions business is our Ongoing Business adjusted operating earnings before income taxes. In the third quarter, these earnings grew to $307 million, which is up approximately 4% over the third quarter of 2012.



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Our Ongoing Business annualized ROE for the first nine months of 2013 improved to 9.9%, 160 basis point improvement from our full year 2012 ROE of 8.3%. In a moment, Alain will provide more detail on our ROE improvement initiatives.

Turning to our Closed Block Variable Annuity book, as you know, our hedging program is designed to protect regulatory and rating agency capital from market movements rather than minimize GAAP earnings volatility. We continue to actively manage the Closed Block Variable Annuity book in line with our strategy.

As we move to slide five, you will see how we continue to leverage our leadership positions in the attractive market segments to deliver diverse earnings. In the first nine months of 2013, we delivered $888 million in pre-tax adjusted operating earnings.

Approximately 74% of the operating earnings came from Retirement Solutions and Investment Management, which are our least capital-intensive businesses. Retirement and Investment Management achieved $234 million and $1.8 billion in net flows respectively in the third quarter. As we've noted before, we serve large institutional clients and net flows will vary from quarter-to-quarter. As we continue with our re-pricing initiative, we're pleased with the clients we're retaining and the new clients who are choosing our value proposition.

Total assets under management and administration grew to a record $494 billion, up from $461 billion at the end of 2012. The remaining 26% of our operating earnings came from our Insurance Solutions business. We continue to reposition our Individual Life business with a focus on less capital-intensive products and we're also investing in our Employee Benefit business. Overall, we remain confident that we're well positioned in the right markets to generate steady growth.

On slide six, our Ongoing Business adjusted operating ROE for the first nine months of 2013 was 9.9% on an annualized basis, up 160 basis points from full year 2012. This is a strong improvement. It reflects our ability to execute on our initiatives, to achieve our plan of an average of 110 basis points on an annual improvement in our ROE. We're committed to that plan.

Now I'll turn it over to Alain for more details about our ROE and ROC improvement program. Alain?

## Alain M. Karaoglan

*Chief Operating Officer, Director & Executive VP, ING U.S., Inc.*

Thank you, Rod, and good morning, everyone. As you know, we are executing on more than 30 initiatives to improve our return on equity and return on capital. And these initiatives fall into three categories: margin initiatives, growth initiatives and capital initiatives. And as I have noted before, our execution is what will enable us to achieve the return on equity and return on capital improvement objectives that we have discussed with all of you.

On slide eight, you see that our total Ongoing Business return on capital improved to 8.3% in the first nine month of 2013. That's up 110 basis points from 7.2% in 2012. The improvement was driven by our execution in the three categories.

First, we are focusing on improving margins through the re-pricing actions, the run-off of our sub-profitable businesses, and aligning costs with lower levels of sales in certain capital-intensive products. In addition, margins have benefited from lower administrative expenses, in line with our plan to achieve $100 million of cost savings over the next several years.


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Second, we are focused on growth. We have generated higher fee-based margins on assets under management and administration, which have grown to $494 billion from $461 billion since year-end 2012. This was due in part to positive net flows from Retirement and from Investment Management.

Third, we are focused on the best use of capital. We have made further progress in shifting the composition of our product portfolio to be less capital-intensive and more fee-based. There were a few items in the first half of 2013 that have favorably impacted our return on capital year-to-date performance. These included a true-up in the variable compensation accrual, recordkeeping change orders, and favorable prepayment income.

Moving forward, we will build upon the already strong improvement we have reached thus far to achieve our return on capital target of 10% to 11% by 2016.

Now let me give you a few examples to demonstrate how our initiatives are making an impact in each of our businesses. And let's begin with the Retirement on slide nine. Retirement improved its return on capital to an annualized 8.9% in the first nine months of the year. That is up 170 basis points from 7.2% in 2012. We are benefiting from the actions we have taken to improve margins, such as through the lowering of crediting rates and to improve our capital position, such as through reinsurance actions.

We are also seeing results from our growth initiatives including improving profitability through the pricing actions we have taken this year and by winning new mandates at our internal rates of return. A notable example from the third quarter is directly related to our breadths of expertise in handling large complex, defined contribution plans as well as understanding the small end of the market.

As a result, we were recently selected to become the service provider for the ADP TotalSource Retirement Savings program. A multi-employer arrangement that includes $2 billion in asset across 2,800 plan sponsors with more than 57,000 participants. And of the $2 billion in asset associated with this win, $1 billion went to Investment Management funds.

This is a significant win that demonstrates our ability to work across business line, deliver value to clients and drive greater value for ING U.S. as a whole.

Moving to slide 10. Annuities improved its return on capital to an annualized 6.8% in the first nine months of 2013. That is up 90 basis points from 5.9% in 2012. As you know, we are running off our less profitable business such as our multi-year guarantee annuity and annual reset blocks but we are also growing sales of our mutual fund IRA custodial product called Select Advantage. This is a capital efficient fee based product that clearly meets a growing customer need. Net flows for Select Advantage were more than $400 million in the first nine months of 2013 and key to Select Advantage growth has been an increase in the number of regional wholesalers supporting sales of this product.

As we move to slide 11, recall that for Investment Management, we focus on operating margin rather than return on capital because this business is not a capital intensive business. And Investment Management's operating margin increased to 26.5% in the first nine month of the year, up from 24.6% in full year 2012 and our 2012 results were helped by strong returns on invested capital.

Excluding those investment returns, our margin improved significantly to 24.1% from 18.4%. One of our key initiatives for operating margin improvement is to leverage our strong investment performance and improve our sales force productivity in higher fee asset categories. The 82% and 89% outperformance of benchmark figures for fixed income and equity assets noted on the slide are up from 54% as of year-end 2012 and 74% respectively.


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During the third quarter, we generated investment-only sales in the defined contribution market of more than $400 million, including large cap growth, mid-cap growth and senior loan mandates for institutional clients. And as I mentioned a moment ago, the recent ADP win in Retirement included $1 billion in assets for Investment Management.

Turning to slide 12, Individual Life improved its return on capital to an annualized 4.8% in the first nine months of 2013. That is up 50 basis points from 4.3% in 2012 as results benefited from favorable mortality in the third quarter. To continue improving returns for Individual Life, we are focusing on less capital products such as index universal life and aligning costs with our new levels of sales. For example, administrative expenses were approximately 13% lower in the first nine months of 2013 compared with the same period last year. These actions will enable us to offer products that provide valuable returns and help the underinsured middle market meet their financial protection needs.

Turning to slide 13, the return on capital of employee benefits has increased to an annualized 17.4% in the first nine months of 2013. That is up 50 basis points from 16.9% in 2012. As you know, we are investing in our Employee Benefits business, which can provide higher return and capital generation and it's a business that is less sensitive to interest rates.

In Stop Loss we have continued to achieve our profitability targets. At the same time, we are investing in sales force training related to prospect identification and information collection. This will further improve our momentum for Stop Loss while maintaining solid risk selection and underwriting.

In Group Life, mortality was unfavorable this quarter and slightly above our targeted range. This was due to several large claims in the quarter. In voluntary benefit sales are up 12% in the first nine months of 2013 compared with the same period last year. And this continues to represent a significant growth opportunity for us.

So, overall we are pleased with the progress we've made toward achieving our long-term return on equity targets. By continuing to focus on the strong execution of our return on capital initiatives, we can continue our positive momentum.

Now, let me turn it over to Ewout who will go into our financial results into more detail. Ewout?

## Ewout L. Steenbergen

*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

Thank you, Alain and good morning. Let me take you through our key financial metrics for the third quarter. So let's start on slide 15. I will walk you through this quarter's reconciliation from the Ongoing Business adjusted operating earnings to net income, and all information presented here is on an after-tax basis.

Starting on the left, the Ongoing Business adjusted operating earnings were $199 million after positive DAC/VOBA unlocking and the net partnership income that Rod mentioned earlier, the ongoing Business operating earnings were $315 million, then adding corporate expenses of $41 million which are mostly interest expenses, and operating earnings of $9 million from the Closed Block Institutional Products and Other Closed Blocks, we had operating earnings of $283 million in the quarter.

Moving to the below the line items, our Closed Block Variable Annuity segment, including non-performance risk had a loss of $109 million, reflecting an accounting asymmetry between GAAP and statutory results. The impact of non-performance risk was minimal this quarter. And then lastly, in addition to the $42 million in net realized gains this quarter and some other items, we also had a $139 million difference between the assumed 35% tax rate,


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and our actual tax rate which was close to zero. And this brings us to a net income to common shareholders of $347 million.

In slide 16, as you know, we are managing our business on the basis of three main drivers of operating revenues. Beginning with underwriting, revenues in the quarter saw a slight decline driven by unfavorable mortality in Group Life which was partially offset by better mortality results in Individual Life.

Excluding the net partnership income, investments spread and other investment income came down slightly during the third quarter as lower as investment income was partially offset by some crediting rate actions we have taken.

And then finally, we saw an increase in fee-based margins, mostly in Retirement and Investment Management businesses, and these were driven by the positive net flows and also helped by equity market appreciation.

Moving to slide 17, we conducted our annual review of assumptions and projection model inputs during the third quarter. The total company impact was a pre-tax loss of $91 million on a GAAP basis and a decrease in statutory reserves of $367 million, which is a positive development.

Focusing on our Closed Block Variable Annuity segment for a moment, you can see that the impact of policyholder behavior assumption changes on lapse and annuitization was a loss of $85 million pre-tax on a GAAP basis and on a statutory basis, reserves increased by $56 million. Mortality assumption and projection mobile input changes resulted in a $100 million pre-tax loss on a GAAP basis and a $423 million decrease in statutory reserves. In a moment, I will cover our hedge program performance as well as the continuing improvement in several Closed Block Variable Annuity metrics this quarter as we continued to run-off this block.

In slide 18, you can see that the strong, Ongoing Business, adjusted operating earnings were in part due to lower administrative expenses. The 4% year-over-year improvement in earnings was achieved in light of lower investment income due to approximately $800 million lower capital in the Ongoing Business.

On the expense side, I should note that the cost reductions that we are executing are offset here by higher variable expenses related to higher sales and other higher volume effects from some of our businesses.

In slide 19, I will quickly give you some color on underlying performance in each of our Ongoing Businesses. Retirement achieved another quarter of positive net flows, which were $234 million in the quarter based on sales that are priced at or above our 12% target return level. We generated strong net flows in our stable value business, primarily due to a large deposit from an existing record keeping client. And as Rod noted earlier, we serve large institutional clients and as is illustrated in this chart, net flows will vary from quarter-to-quarter especially with the pricing discipline we apply.

In slide 20, turning to Annuities, as Alain mentioned, we have continued to generate net flows into our Select Advantage mutual fund custodial product where we earn attractive margins. At the same time, we saw a continuation of the outflow of the low or negative margin products, such as the annual reset and the multi-year guaranteed annuities. These outflows also help in reducing the capital health for this business.

Slide 21, Investment Management net flows in the quarter were $900 million of Affiliate Sourced assets and $700 million of Investment Management Sourced assets for a total of $1.6 billion. This reflects the ADP new business win that Alain referenced earlier, which was $1 billion in Retirement assets invested with Investment Management.


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In addition, we had non-ING U.S. sub-advisor replacements of approximately $900 million and you can also see that outflows for the Closed Block Variable Annuity funds that are managed by Investment Management were roughly $600 million. When you include the sub-advisor replacements and the Closed Block Variable Annuity outflows, the net flows were in total $1.8 billion for the quarter.

Slide 22, this slide shows that we are continuing to execute on our strategy to shift our Individual Life business to less capital intensive products with sales of fixed guaranteed products declining from a year ago. Equally important, we have right-sized our expenses relative to the new scale of the Individual Life business.

In slide 23, in Employee Benefits, we saw continued strength in our loss ratio for Stop Loss at 72.8%. The Group Life loss ratio was within normal volatility at 82.1%, slightly above our targeted range of 77% to 80% as we had several large claims in the third quarter. Total sales were up year-over-year. Sales in this business are lumpy with the majority of sales occurring in the January and July renewal periods.

Then turning to slide 24, this chart illustrates our hedge performance in the Closed Block Variable Annuity segment. In the quarter, our hedge program has offset the change in statutory reserve liability as a consequence of the equity market movements. During the quarter, a part of the $400 million net impact was used to reduce letters of credit to zero. The net amount at risk for the living benefits declined by $800 million during the quarter to $3.0 billion, and that is now lower than the $3.5 billion in statutory reserves for living benefits. And our total available resources for the Closed Block Variable Annuity segment are $4.8 billion.

The net outflows were $900 million for the quarter, which leads to an 8.6% annualized net outflows as a percentage of the beginning of period assets. Excluding payout annuities, the net annualized outflows would be 9.7%. At the lower part of the page, you see the new sensitivity tables for the end of the third quarter for both regulatory capital as well as GAAP earnings, for equity markets and interest rate movements.

And then finally, slide 25. You can see that our combined estimated risk based capital ratio at the end of the third quarter was very strong at 470%. The RBC ratio improved relative to the second quarter primarily reflecting statutory income earned during the quarter.

On the right side of the slide, the debt-to-capital ratio at the end of the second quarter declined and is now 24.5% and it's slightly below our leverage ratio, our target leverage ratio of 25%. 19.2% of this ratio is senior debt and 5.3% is junior subordinated debt.

So in summary, building on the momentum we have achieved in the first half of this year, we delivered solid financial results this quarter as we continue to focus on increasing margins, running off less profitable businesses and protecting regulatory and rating agency capital in the Closed Block Variable Annuity.

And with that, I will turn it back to the operator, Emily, so we can take your questions.

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## Rodney O. Martin

*Chairman & Chief Executive Officer, ING U.S., Inc.*

Emily, it's Rod Martin speaking. I want to clarify one number that I misspoke about on slide four. The slide is accurate. The very first bullet point, after-tax operating earnings of $283 million or $1.08 per diluted share, apparently, I said $238 million versus $283 million. For that, I'm sorry. Back to you, Emily.


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# QUESTION AND ANSWER SECTION

**Operator**: Thank you. We will now begin the question-and-answer session. [Operator Instructions] The first question is from Ryan Krueger of Dowling & Partners. Please go ahead.

Ryan Krueger
*Analyst, Dowling & Partners*

Q

Hey, thanks. Good morning. I had a question on the investment spread in the Retirement business. I guess, first of all, if I look at the reported amount of $181 million, I believe that included about a $15 million benefit from the Lehman Recovery. So if I exclude that it looked closer to about $167 million, which I think compared to about $180 million-ish in the first half of the year. I guess, am I looking at that correctly and if so, what was the driver of that decline?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

Ryan, good morning. This is Ewout. Yes, I can confirm that those numbers are correct. The main drivers of the decline of the investment margin are that we have had elevated a prepayment income during the first half of the year and that is more normalized during the third quarter. And secondly, as we have in our plan, we expect the investment income to come down over time since the reinvestments are still down at a lower level than the current portfolio yield. So, this is really the impact of the low rate environment. It is less than what we assumed a year ago. But clearly, there's still a negative impact from that over time. So those are the two main drivers why the investment spread in Retirement is lower than what you have seen in previous quarters.

Ryan Krueger
*Analyst, Dowling & Partners*

Q

Okay, thanks. That's helpful. And then – and just in terms of the statutory reserve benefit from the annual actuarial review, can you talk a bit about the drivers of that? I guess, it sounded like a lot of it may have been improved mortality projections but I guess I wouldn't have necessarily thought that that would have caused a huge benefit to variable annuity reserves. So could you talk about that a bit?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

There's three elements why you see the large decrease in statutory reserves. The first is what we have done, we have done refinements of the NAIC mandated scenarios to really align it with management best estimates. So that is one element. The second element is we are updating all the projection model inputs especially related to macroeconomic factors. Think about the rate environment. So that is the second reason.

And the third is we have implemented an assumption change for mortality improvement. On a statutory basis, we had already assumed mortality improvement for the living benefits. It's now being introduced for the death benefits and a mortality improvement for death benefits leads also to a positive assumption update. So those are the three main drivers, why you see a positive impact on a statutory basis.

Ryan Krueger
*Analyst, Dowling & Partners*

Q

Excellent. And then, just lastly, did that impact the RBC ratio at all or was that all in the captive entity?


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Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*
A

Almost all is captured in our offshore entity, so is not reflected in the RBC ratio, which we have disclosed to you.

Ryan Krueger
*Analyst, Dowling & Partners*
Q

Thank you.

**Operator**: The next question is from Erik Bass of Citigroup. Please go ahead.

Erik J. Bass
*Analyst, Citigroup Global Markets Inc. (Broker)*
Q

Hi. Thank you. Can you just talk a little bit about the capital generation year-to-date? And I guess with the RBC ratio at 470%, does this suggest that you're starting to build excess capital sooner than you had anticipated?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*
A

Good morning, Erik. Yes, that was an understandable question that you would ask. If you look at the RBC ratio 470%, if you calculate a dollar impact, it's approximately $670 million above our target 425% RBC level. And then we – as you have also learned, we have seen some favorability on a statutory basis in our offshore entity. So clearly, from that angle, you could say that we're making good progress towards the targets we have set.

At the same time, if you look at where we are today, it's just a little bit over half a year after the IPO. We had even a primary as part of the IPO and we are not at this moment, at a point that we think we should change the guidance with respect to our excess capital generation. So the guidance is still the same. We expect to generate $1.2 billion to $1.4 billion mostly in 2015 and 2016. The natural moment what we will do is at year end we will update our financials. We'll look at the financial statements on a GAAP and on a statutory basis. We'll look at our new projections and then somewhere in spring of next year we can come back to the market with new guidance. So clearly, we made good progress with respect to the capital generation, but new guidance will be provided in spring of next year.

Erik J. Bass
*Analyst, Citigroup Global Markets Inc. (Broker)*
Q

Okay. That's helpful. And then, if I could ask just one on the tax assets. I mean, it looks like you did get a benefit from using the deferred tax assets this quarter. And then, just when do you expect to review the valuation allowances that you're currently holding against the tax assets and maybe under what scenario would you be able to release all or a portion of the allowance?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*
A

For the time being, we expect to release tax valuation allowances or to setup tax valuation allowances on the basis of the actual income or loss we generate during the quarter itself. So that will drive the effective tax rate to close to zero for the foreseeable future. And we cannot emphasize that enough that that is a very important value driver for the company that in our recalculations, we assume the 35% tax rate, but in reality, the effective tax rate is close to zero.


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So it might be, at some point further in the future when our projections will support sufficiently that we don't need to hold the tax valuation allowances anymore then we can do a larger release. You also have to show a couple of periods of income before you can really make that step. So I think for the next few quarters, you should not expect that there will be a large movement with respect to our tax valuation allowance.

Erik J. Bass
*Analyst, Citigroup Global Markets Inc. (Broker)*

Q

Okay. Thank you.

**Operator**: Next question is from Chris Giovanni of Goldman Sachs. Please go ahead.

Christopher A. Giovanni
*Analyst, Goldman Sachs & Co.*

Q

Thanks so much. Good morning. Just one follow-up to the capital piece, you talked about RBC. Obviously, the Corporate segment has had capital allocated to it, it increased from about $900 million last quarter to $1.5 billion this quarter. Can you touch on kind of that delta there? And obviously from a liquidity standpoint, it looks like relative to your interest expense, you have a fair amount up at the Corporate level there. So is that incremental may be free cash flow that we should be thinking about?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

Good morning, Chris. Indeed, if you look at page seven of the statistical supplement, you see the capital development in each of our segments including the Corporate and Other Closed Block segment. How you should think about that particular number, which is now $1.472 billion at the end of the quarter is, that it is an aggregation of several items. So what you see there is the holding company liquidity that's the 24-month holding company liquidity that's captured there, that's the $450 million slightly higher at the end of the third quarter. It also contains all the RBC ratio that is over the 425% level. So we allocate capital to each of our Ongoing Business segments on the basis of an RBC of 425%. If the actual RBC is higher, that is basically then showing up in the Corporate segment.

And then, you should also see if there's any other capital development that is not needed in the segment, including the Closed Block Variable Annuity that it will show up in the Corporate segment. There's other items there – there is the capital for the Other Closed Blocks, there is some other intangibles and other items. But in general, you can think about it. This is the holding company liquidity plus the excess RBC over the 425% in each of our segments.

Christopher A. Giovanni
*Analyst, Goldman Sachs & Co.*

Q

Understood. Okay. And then staying within Corporate, I guess, the other line showed a loss of $7.4 million this quarter, when it had been running consistently pretty positive. So wondering kind of what drove that negative variance this quarter and how should we thinking about that as we move forward?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

The line Corporate Other is a line that contains several items. So, for example, what is captured there is some investment income on our Corporate investment portfolio. This particular quarter, we had also some non-recurring accrual adjustments and catch-ups, including variable compensation and some litigation matters. So they were all not large enough to spike out as notable items. So indeed there were some more notable items on the


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negative side, smaller ones on that particular line. But I would really recommend you to look at that relative to the large notable items with respect to the DAC unlocking and the partnership income and the positive we had in respect to our overall performance during the quarter.

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Christopher A. Giovanni
*Analyst, Goldman Sachs & Co.*
Q

Okay. And then just one last quick one, if we think about how you've historically calculated the ROE, you've assumed 25% leverage and a 5.5% kind of yield on the debt. The leverage is now kind of below your target, yield's probably favorable as well. I mean, how should we be thinking about kind of the definition and the calculation of the ROE given those two drivers?

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Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*
A

So, Chris, we have made one change in our methodology to calculate the ROE during the quarter and that relates to the interest expense on our debt. So, as you know, we have really finished our total recapitalization of the company that has been done in a very successful way. And the interest expense that we are paying today on our debt is closer to 5.3% and that compares to the 5.5% we had before as an assumption in these calculations.

So going forward prospectively, we will update our calculation. And for the next quarters, you will see the 5 .3%. So, we don't change everything we have published in the past. But going forward, we will apply more the actual interest expense on our debt to the 5.3%. In respect to the leverage ratio, we're not planning to make an update, so we keep the 25% despite the fact that our leverage ratio is now lower. That can move around a little bit, so we don't want to adjust that every quarter. So, that's why we keep that constant at a 25% leverage ratio.

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Christopher A. Giovanni
*Analyst, Goldman Sachs & Co.*
Q

Thanks so much.

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**Operator**: The next question is from Jeff Schuman of KBW. Please go ahead.

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Jeffrey R. Schuman
*Analyst, Keefe, Bruyette & Woods, Inc.*
Q

Thank you. Good morning. I want to do variable annuities first. If we look through the actuarial assumption impact, it looks like net income would have been positive this quarter, which we don't normally expect in an up market quarter. So, can you give us a little perspective on that outcome, please?

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Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*
A

Sure. There were four reasons why the GAAP result for the Closed Block Variable Annuity was more favorable than the expectations on the basis of the earnings of risk sensitivity table we have provided to you. The first is we have seen that our funds actually outperformed the underlying indices that we are tracking. So we have seen positive tracking error there. We have also seen a slightly positive tracking error for the rho hedges.

Then the third is that we have seen a reduction of actual and implied volatility. So that was also a clear, positive effect. And the fourth reason is the secondary order effect of the assumption change. And let me elaborate a bit on that. So what is happening, you implement the assumption change retroactively at the beginning of the quarter, the first day of the quarter, which means that the liabilities to reserves should be higher, retroactively and with the


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assumption update. But you have not had adjustments to your hedge program during the third quarter in hindsight.

So in fact, you could say we were slightly under-hedged relative to the liabilities we are protecting during the quarter and there we have an upmarket. So underhedged and an upmarket led to another positive deviation. So those were the four main drivers why we saw a better result of the Closed Block VA than the underlying expectations.

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**Jeffrey R. Schuman**
*Analyst, Keefe, Bruyette & Woods, Inc.*

Q

The follow-up there. So the tracking errors or the basis of mismatch I guess worked in your favor this quarter. I'm just wondering sort of longer term and thinking maybe more about economics instead of the accounting. I mean, is there a sufficient basis risk that they could bite you at some point? Is that something we should be concerned about?

---

**Ewout L. Steenbergen**
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

This is moving around quarter-to-quarter. In fact, we saw unfavorable tracking error during the second quarter. Very clearly, we are trying as much as possible to tailor our hedge program, to really match the underlying funds and to have the hedge program really minimize the basis risk.

The point is that some of those funds are actively managed funds and you can't never have here a perfect hedge that is really matching exactly the underlying fund movements. So, you're right, this can move around. Some quarters it's positive, the other quarters it's negative, but clearly the focus of the whole hedge program is to minimize that basis risk as much as possible.

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**Jeffrey R. Schuman**
*Analyst, Keefe, Bruyette & Woods, Inc.*

Q

Okay. And one other area if I may. The Individual Life sales, it looks like you've been very successful in bringing down the sales of the products that you don't want to sell. I guess it's less clear that you're getting momentum really growing the other sales. I mean is – do you have kind of a timeline for when that might kind of accelerate?

---

**Rodney O. Martin**
*Chairman & Chief Executive Officer, ING U.S., Inc.*

A

Yes, good morning. It's Rod speaking. So, as you noted, we have made a very conscious choice as previously communicated to exit or de-emphasize certain products and emphasize others. By way of example, our indexed Universal Life portfolio, and we are making progress. It is slower than we anticipated, but we are making some progress. So, the piece that we were focusing on was de-emphasizing the higher consumptive capital-intensive businesses and we're at a run rate now, roughly in the $120 million or $130 million run rate. And we're very aggressively, as Alain pointed out in his comments, adjusting our expenses to be aligned with that run rate. But we are actively pursuing growing the index in the middle market term business, index Universal Life portfolio and the middle market term business and we think we've got an excellent portfolio. And certainly we'll keep you posted and you'll see the results as we move through this quarter-to-quarter.

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**Operator**: The next question is from Jimmy Bhullar of JPMorgan. Please go ahead.

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**Jimmy S. Bhullar**
*Analyst, JPMorgan Securities LLC*

Q

Hi. First I had a question on the Retirement business. Just wondering if you could discuss how far along you are on your re-pricing initiative and part of the reason I'm asking is if you look at fee income in Retirement, it's up about 5% from the third quarter of last year, 1% sequentially it's lower than the AUM growth that you've shown. So, obviously, there's probably a mixed shift within there also, but that's just if you could talk about how far long you are on repricing and when do you expect that to be done?

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**Rodney O. Martin**
*Chairman & Chief Executive Officer, ING U.S., Inc.*

A

Jimmy, it's Rod. Good morning. As you and others call, this book of business is a five or six year journey. We're about 15 to 18 months in that journey. We feel very positive about our ability to increase our ROC while we've been repricing our book of business and delivering what we believe is differentiated value. We gave you a couple of data points. So the first nine months of the year, we generated more than $3 billion of full service transfer deposits at IRRs at or above our target of 12% and that's a 25% increase on a year-to-date basis over 2012.

As we have signaled today and in previous calls, we are focusing on accomplishing ROC, a growth in ROC at or above our targets. We are in a large institutional business. We will see from period-to-period differentiation as we move through this. And again, there's not a lot we can do about advancing our book of business that renews over the next four plus years. It's just simply a journey that we're going to go on, and that's why we will see this movement from period to period.

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**Jimmy S. Bhullar**
*Analyst, JPMorgan Securities LLC*

Q

Okay. And then on – you mentioned about half of the ADP Retirement assets going to your own Investment Management business. Maybe talk a little bit about the percentage of Retirement assets that are being managed by the asset management side now versus maybe two, three years ago and where you expect that number to go?

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**Alain M. Karaoglan**
*Chief Operating Officer, Director & Executive VP, ING U.S., Inc.*

A

Good morning, Jimmy. Yes. The ADP win was a significant one in terms of showing the capabilities that we bring and the value added that we bring for the client. A client that needed to be serviced on the large hand, on the small hand and also we had to win this Investment Management mandate with our capabilities.

So if you look at the proprietary share within Retirement, one thing you have to keep in mind is the breadth of our franchise is different than other companies you may be looking at. So we're in the corporate markets, we're in the tax exempt market and we're in the record keeping business. And depending on what number you look at, Jimmy, you may come to a different percentage. So if we look at all the three combined, we're at around 18% including the record keeping, the corporate and the tax exempt market.

And within our plans, we don't have any specific metric to increase that over the next few years. But that is – so our plan do not contemplate that ratio going up, but this is potential upside that we have to the extent that we are successful in increasing that ratio over the next few years.

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**Jimmy S. Bhullar**
*Analyst, JPMorgan Securities LLC*

Q


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Okay. And then lastly, just – there's been a few companies that have actually decided to consolidate their captives and bring them onshore and I'm wondering if you have given thought to that? And also related to that, what would your RBC ratio be if you were to consolidate your offshore entity?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

Jimmy, good morning. This is Ewout. The short answer is we are always exploring all options to optimize our structure. Let me give you a little bit broader answer, and a little bit more context. If you go back, the last year, we have had very active and constructive discussions with our regulators in preparing for the IPO. We have had received all the approvals for the IPO including the reset to zero, the extraordinary dividends and so on. So we are very comfortable that our structures today are in full compliance with all applicable regulation. So, we are as anybody exploring all options. If there is anything that we can mention to you, we will come back to you at the right point in time. So, no conclusions have been drawn at this moment.

With respect to the impact, our offshore entity holds the full AG43 reserves. As well, we have the full CTE (95) S&P level in terms of total assets requirement in our offshore entity. The rating agencies apply a look-through, so there won't be any difference.

The impact if, and this is hypothetically, if you would, onshore is very much dependent on the circumstances. You have heard several players speaking about modified GAAP, so it's very hard to give you a precise answer on what would be the impact. But overall, given the level of capitalization, the level of assets we have put aside for our Closed Block Variable Annuity, we think an onshoring event would be absolutely manageable for us as a company.

**Operator**: Our next question is from Tom Gallagher from Credit Suisse. Please go ahead.

Tom G. Gallagher
*Analyst, Credit Suisse Securities (USA) LLC (Broker)*

Q

Good morning. Wanted to ask a few questions about the VA Closed Block. The $4.8 billion of available resources, if I deduct the $3.5 billion of living benefit reserves, I get $1.3 billion. Of that $1.3 billion, how much would be surplus versus other reserves like death benefit reserves? That's my first question.

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

Good morning, Tom. The calculation you have made is correct. The difference, the $1.3 billion, approximately $800 million refers to the statutory reserves for death benefits. And then, the remainder is applicable to cash flow testing reserves and other assets we hold. We are not going to give you a breakdown of that number, but the remainder is cash flow testing reserves and other assets we hold.

Tom G. Gallagher
*Analyst, Credit Suisse Securities (USA) LLC (Broker)*

Q

So, Ewout, so all of the available resources I should be thinking about as reserves and not necessarily surplus?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

No. I think if I say cash flow testing reserves and other, you should see it from a more holistic perspective. But we are very careful to earmark anything as excess today. I think that's in line with the other question that was raised a


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couple of minutes ago. We think it's too early to draw conclusions at this moment what we should earmark as excess versus what we really need to support this book in the future.

We will come to that assessment after year-end, and we will come back to you with any further answer on that question. So it's just too premature at this moment, Tom. It's an understandable question and we promise to you, we will come back to you in the spring of next year with a precise answer.

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**Tom G. Gallagher** Q
*Analyst, Credit Suisse Securities (USA) LLC (Broker)*

Got it. And then just as a follow-up, the $4.8 billion of available resources, can you remind me at this point what amount of those are hard assets versus LOCs?

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**Ewout L. Steenbergen** A
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

This is currently backed fully by hard assets. So there is no LOCs outstanding anymore.

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**Tom G. Gallagher** Q
*Analyst, Credit Suisse Securities (USA) LLC (Broker)*

So the $4.8 billion would be all hard assets?

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**Ewout L. Steenbergen** A
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

Yes, correct.

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**Tom G. Gallagher** Q
*Analyst, Credit Suisse Securities (USA) LLC (Broker)*

And then you still have the LOC, I believe as part of your hedge program that you can draw down on, is that the right way to think about it?

---

**Ewout L. Steenbergen** A
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

Yes. It could be. At certain moments in the future, when there is a certain mismatch between the different capital requirements, the statutory versus the rating agency requirements. There could be an ability that we have to draw on the LOC so the facility is outstanding standby, and we can draw upon that. But as of the end of the third quarter, the $180 million of LOCs that were outstanding at the end of the second quarter were completely brought down back to zero.

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**Operator**: The next question is from Doug Mewhirter of SunTrust Robinson Humphrey. Please go ahead.

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**Doug R. Mewhirter** Q
*Analyst, SunTrust Robinson Humphrey*

Hi, good morning. Just had two questions, one on Retirement and one on the Annuities business. First, you've had a lot of – you gave me a lot of great color on the fund flows and that's a great win with the ADP account. I did notice the flows have been positive but it's decelerating. The rate of growth has slowed over the past three quarters, so 6.3% in first quarter, 1.8% in the second quarter and now 1% in the third quarter.


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First, is there any seasonality I should be thinking about? And second, is that deceleration as a result of your re-pricing? Do you expect I guess a tick back up in that? Do you have anything in the hopper that would reverse that decelerating trend? Any more details you'd give around that?

Rodney O. Martin
*Chairman & Chief Executive Officer, ING U.S., Inc.*

A

It's Rod again and I'm going to really bring you back to what we've discussed just a moment ago. Our entire focus on this existing book of business is re-pricing at or better than 12% as we move through this. And I want to strongly emphasize we're being very disciplined and we're pleased with the response to it, which doesn't mean that we're winning every case and we are walking away from those that we're not. And that's what you will see movement period-to-period.

And we cannot accelerate a four-year book of business that's remaining faster than that. That's – we will just be having the same conversation about the renewal book for the next four or so years as we go through this.

The comment that Alain made about the ADP case is a new piece of business that met or exceeded those targets and is the combination of those things driven back to our ROC and ultimately, ROE improvement over that period of time that we're really trying to drive. That's where our attention is and that's how we're defining success as we move through this.

Doug R. Mewhirter
*Analyst, SunTrust Robinson Humphrey*

Q

Thanks for that answer. My question about Annuities regarding the spread, you have commented that the – your spread has declined sequentially and I think that is – a lot of that is frankly happening in the industry.

Given the fact that Annuities are fairly capital intensive, it's not a really – area of really tight focus for growth. Why wouldn't you be more, I guess, aggressive with crediting rates especially in the higher capital intensive products where you would be – you'd be willing to give up more business if you can get the spread back moving back in the right direction?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

So, this is Ewout. Let me try to give you some more color about the Annuities. First of all, you will – two comments. First of all, you will see a decline of the investment spreads according to the planned runoff of some of the underlying blocks. So we will see a decline of the blocks, of the older, multi-year guaranteed annuities where we have very low margins or negative margins. If that block is running off, the absolute magnitude of the spreads will come down. At the same time, we will also release capital there. So the returns on the total annuity block as a consequence of this will go up. So that is the first part of the information I wanted to give to you.

With respect to the crediting rates, the Annuity block is on average somewhere in the mid-60% of the minimal levels we can apply. We cannot bring this fully to a higher percentage of minimum crediting levels at this moment because there is always two limitations. One is regulatory limitations and the other are commercial limitations. So, if we issue new products with very low guaranteed minimum interest rates, think about very low, very low levels.

Commercially, of course we are not bringing those policies to those levels immediately. So, you have to look through here a bit of some older blocks where we're actively trying to manage to be at really minimum crediting levels in some of the newer business we are writing that have guaranteed minimum interest rates that are already


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much lower and were weak from commercial reasons, don't bring it to the absolute minimum levels right now. So, it's a little bit hard to look through those numbers to see those underlying dynamics.

Doug R. Mewhirter
*Analyst, SunTrust Robinson Humphrey*

Q

Okay, thanks for that. That's all my questions.

**Operator**: Okay. Our last question will come from Mark Finkelstein of Evercore. Please go ahead.

Alan Mark Finkelstein
*Analyst, Evercore Partners (Securities)*

Q

Good morning. I wanted to go back to the Closed Block Variable Annuity adjustments that you made. We spend a lot of time thinking about lapse markets rates, et cetera, and what you showed in the quarter was a pretty positive effect for mortality and maybe some other model inputs. And I guess what I'm interested in is does this adjustment have any meaningful effect on your expectations around future cash flows of that Closed Block business?

Ewout L. Steenbergen
*Chief Financial Officer & Executive Vice President, ING U.S., Inc.*

A

Good morning, Mark. With respect to our cash flow models and for the Closed Block Variable Annuity under the different scenarios, as we have shown to the market around the IPO, we're planning to provide an update of that after year end. So once a year, we will provide an update to you and the rest of the market with respect to updates of those scenarios, so you can follow the progress of the book along the way. So, it's a little bit too early to comment on that. The mortality improvement was a positive on a statutory basis, given the fact that we had already assumed mortality improvement for the living benefits and this was for the death benefits. It clearly has had an impact on the capital position of the Closed Block Variable Annuity.

But how that would translate in the longer term cash flow projections, I think it's just too soon to give you any guidance on that but after year end, we will give you the updated scenarios and we can talk a little bit more and provide you more color around that.

Alan Mark Finkelstein
*Analyst, Evercore Partners (Securities)*

Q

Okay. Maybe a question on the Stop Loss business. There's a view out there that over time, you're going to see medical move from, call it DB to DC structure, it's perhaps more fully-insured programs. You look at your sales in the quarter and they are very strong. I'm just curious if you have any updated views on that business in light of healthcare reform and maybe any insight into January 1 renewal.

Rodney O. Martin
*Chairman & Chief Executive Officer, ING U.S., Inc.*

A

Good morning, it's Rod again. In the short-term, we are actually seeing what we think are limited short-term negatives from employers that are focusing more right now on the medical versus Group Life and some of the other voluntary benefits. We think this will cycle as they work through the process that everyone is going through right now.


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Longer term, we actually see some opportunity. I think it strongly reinforces, we've got a leading franchise in Stop Loss with some excellent capabilities and I think the supplement to that of our voluntary capabilities as we push forward is again additive to where we've been thinking about this historically.

So in the short-term, there's less activity by way of example on Group Life and other related benefits because there's more focus by the employers right now on sorting through where they are on the medical piece.

Longer term, we think it is – reinforces strongly our franchise and our capabilities. So we think there's a benefit for us.

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**Operator**: This concludes our question-and-answer session. I'd like to turn the conference back over to Rod Martin for any closing remarks.

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## Rodney O. Martin

*Chairman & Chief Executive Officer, ING U.S., Inc.*

Operator, thank you. We're pleased with the results for the first nine months of the year and the progress we're making with our transformation story. ING U.S. is a premier franchise with leading positions in attractive markets.

This management team is committed to executing in average of 110 basis points of annual improvement in our ROE to reach our goal of 12% to 13% by 2016. We'll continue to build on our solid foundation, which is based on a recapitalized and de-risked balance sheet. Our 7,000 employees are intensely focused on executing our plans to create long-term value for shareholders and achieving our vision to be America's Retirement company. Thank you and good day.

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**Operator**: The conference has now concluded. Thank you for attending in today's presentation. You may now disconnect.

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