

KEMPER Corp  
Form 10-K  
February 12, 2015

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-K

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

For the fiscal year ended December 31, 2014  
OR

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

Commission file number: 001-18298

Kemper Corporation  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

95-4255452  
(I.R.S. Employer Identification No.)

One East Wacker Drive, Chicago, Illinois  
(Address of principal executive offices)  
(312) 661-4600

60601  
(Zip Code)

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$0.10 par value per share	New York Stock Exchange
7.375% Subordinated Debentures due 2054	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller Reporting Company

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

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As of June 30, 2014, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$1.95 billion based on the closing sale price as reported on the New York Stock Exchange. Solely for purposes of this calculation, all executive officers and directors of the registrant are considered affiliates.

Registrant had 51,874,886 shares of common stock outstanding as of February 10, 2015.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on May 6, 2015 are incorporated by reference into Part III.

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### Caution Regarding Forward-Looking Statements

This 2014 Annual Report on Form 10-K (the “2014 Annual Report”), including, but not limited to, the accompanying consolidated financial statements of Kemper Corporation (“Kemper”) and its subsidiaries (individually and collectively referred to herein as the “Company”) and the notes thereto appearing in Item 8 herein (the “Consolidated Financial Statements”), the Management’s Discussion and Analysis of Financial Condition and Results of Operations appearing in Item 7 herein (the “MD&A”) and the other Exhibits and Financial Statement Schedules filed as a part hereof or incorporated by reference herein, may contain or incorporate by reference information that includes or is based on forward-looking statements within the meaning of the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995.

Forward-looking statements give expectations or forecasts of future events. The reader can identify these statements by the

fact that they do not relate strictly to historical or current facts. They use words such as “believe(s),” “goal(s),” “target(s),” “estimate(s),” “anticipate(s),” “forecast(s),” “project(s),” “plan(s),” “intend(s),” “expect(s),” “might,” “may” and other words a similar meaning in connection with a discussion of future operating, financial performance or financial condition. Forward-looking statements, in particular, include statements relating to future actions, prospective services or products, future performance or results of current and anticipated services or products, sales efforts, expenses, the outcome of contingencies such as legal proceedings, trends in operations and financial results.

Any or all forward-looking statements may turn out to be wrong, and, accordingly, Kemper cautions readers not to place undue reliance on such statements, which speak only as of the date of this 2014 Annual Report. Kemper bases these statements on current expectations and the current economic environment. They involve a number of risks and uncertainties that are difficult to predict. These statements are not guarantees of future performance; actual results could differ materially from those expressed or implied in the forward-looking statements. Forward-looking statements can be affected by inaccurate assumptions or by known or unknown risks and uncertainties. Many such factors will be important in determining the Company’s actual future results and financial condition. The reader should consider the following list of general factors that could affect the Company’s future results and financial condition, as well as those discussed below under Item 1A., “Risk Factors,” in this 2014 Annual Report.

Among the general factors that could cause actual results and financial condition to differ materially from estimated results and financial condition are:

Factors related to the legal and regulatory environment in which Kemper and its subsidiaries operate

Developments in, and outcomes of, initiatives by state officials that could result in significant changes to unclaimed property laws, or significant changes to the interpretations of existing laws, and significant changes in claims handling practices with respect to life insurance policies, especially to the extent that such initiatives result in retroactive application of new requirements to existing life insurance policy contracts;

Adverse outcomes in litigation or other legal or regulatory proceedings involving Kemper or its subsidiaries or affiliates;

Governmental actions, including, but not limited to, implementation of the provisions of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (collectively, the “Health Care Acts”), the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “DFA”), the Risk Management and Own Risk and Solvency Assessment Model Act (“RMORSA”) and other new laws, regulations or court decisions interpreting existing laws and regulations or policy provisions;

Uncertainties related to regulatory approval of insurance rates, policy forms, license applications and similar matters;

Uncertainties related to regulatory approval of dividends from insurance subsidiaries, acquisitions of businesses and similar matters;

Factors relating to insurance claims and related reserves in the Company’s insurance businesses

The incidence, frequency and severity of catastrophes occurring in any particular reporting period or geographic area, including natural disasters, pandemics and terrorist attacks or other man-made events;

The number and severity of insurance claims (including those associated with catastrophe losses) and their impact on the adequacy of loss reserves;

Changes in facts and circumstances affecting assumptions used in determining loss and loss adjustment expenses (“LAE”) reserves;



The impact of inflation on insurance claims, including, but not limited to, the effects attributed to scarcity of resources available to rebuild damaged structures, including labor and materials and the amount of salvage value recovered for damaged property;

Developments related to insurance policy claims and coverage issues, including, but not limited to, interpretations or decisions by courts or regulators that may govern or influence losses incurred in connection with hurricanes and other catastrophes;

Orders, interpretations or other actions by regulators that impact the reporting, adjustment and payment of claims;

Changes in the pricing or availability of reinsurance, or in the financial condition of reinsurers and amounts recoverable therefrom;

Factors related to the Company's ability to compete

Changes in the ratings by rating agencies of Kemper and/or its insurance company subsidiaries with regard to credit, financial strength, claims paying ability and other areas on which the Company is rated;

The level of success and costs incurred in realizing economies of scale, implementing significant business consolidations, reorganizations and technology initiatives and integrating acquired businesses;

Absolute and relative performance of the Company's products or services;

Heightened competition, including, with respect to pricing, entry of new competitors and alternate distribution channels, introduction of new technologies, the emergence of telematics, refinements of existing products and the development of new products by new and existing competitors;

Factors relating to the business environment in which Kemper and its subsidiaries operate

Changes in general economic conditions, including, but not limited to, performance of financial markets, interest rates, inflation, unemployment rates and fluctuating values of particular investments held by the Company;

Absolute and relative performance of investments held by the Company;

Changes in industry trends and significant industry developments;

Changes in capital requirements, including the calculations thereof, used by regulators and rating agencies;

Regulatory, accounting or tax changes that may affect the cost of, or demand for, the Company's products or services or after-tax returns from the Company's investments;

The impact of required participation in windpools and joint underwriting associations, residual market assessments and assessments for insurance industry insolvencies;

Changes in distribution channels, methods or costs resulting from changes in laws or regulations, lawsuits or market forces; and

Increased costs and risks related to information technology and data security, including, but not limited to, identity theft and the prevention of, or occurrence of, disruption of services.

Other risks and uncertainties described from time to time in Kemper's filings with the U.S. Securities and Exchange Commission ("SEC").

Kemper cannot provide any assurances that the results contemplated in any forward-looking statements will be achieved or will be achieved in any particular timetable or that future events or developments will not cause such statements to be inaccurate. Kemper assumes no obligation to correct or update any forward-looking statements publicly for any changes in events or developments or in the Company's expectations or results subsequent to the date of this 2014 Annual Report. Kemper advises the reader, however, to consult any further disclosures Kemper makes on related subjects in its filings with the SEC.

## PART I

### Item 1. Business.

Kemper is a diversified insurance holding company, with subsidiaries that provide automobile, homeowners, life, health, and other insurance products to individuals and businesses. Kemper's annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments thereto are accessible free of charge through Kemper's website, kemper.com, and as soon as reasonably practicable after such materials are filed with, or furnished to, the SEC.

#### (a) GENERAL DEVELOPMENT OF BUSINESS

##### Issuance of Subordinated Debt

On February 27, 2014, Kemper issued \$150.0 million of its 7.375% subordinated debentures due February 27, 2054 (the "2054 Subordinated Debentures"). The 2054 Subordinated Debentures are unsecured and are subordinated and junior to the senior indebtedness of Kemper. Interest on the 2054 Subordinated Debentures is payable quarterly. As long as no event of default has occurred, Kemper may defer interest payments on the 2054 Subordinated Debentures for up to five consecutive years without giving rise to an event of default. During a deferral period, interest will continue to accrue at the stated interest rate compounded quarterly. Kemper is permitted to redeem some or all of the 2054 Subordinated Debentures on or after February 27, 2019, at a redemption price that is equal to their principal amount plus accrued and unpaid interest. Kemper is permitted to redeem the 2054 Subordinated Debentures in whole, but not in part, at any time prior to February 27, 2019, within 90 days of the occurrence of certain tax events or rating agency events, at specified redemption prices.

##### Kemper Common Stock Repurchases

On August 6, 2014, the Board of Directors approved a new common stock repurchase program (the "2014 Repurchase Program") under which Kemper is authorized to repurchase up to \$300 million of its common stock and terminated Kemper's remaining authorization under a repurchase program previously approved on February 2, 2011 (the "2011 Repurchase Program").

##### Agreement to Acquire Alliance United Group

On December 10, 2014, Kemper entered into a definitive agreement to acquire Alliance United Group and its wholly-owned subsidiaries, Alliance United Insurance Company ("AUIC") and Alliance United Insurance Services ("AUIS"), in a cash transaction valued at approximately \$70 million. Kemper expects to close the transaction in the first half of 2015, subject to approvals by insurance regulators and the satisfaction of other customary closing conditions. Following the closing of the transaction, Kemper plans to contribute approximately \$75 million of capital to support AUIC's book of business. AUIC is amongst the top writers of nonstandard personal automobile insurance in California and had more than \$300 million of direct written premiums in 2014.

#### (b) BUSINESS SEGMENT FINANCIAL DATA

Financial information about Kemper's business segments for the years ended December 31, 2014, 2013 and 2012 is contained in the following sections of this 2014 Annual Report and is incorporated herein by reference: (i) Note 17, "Business Segments," to the Consolidated Financial Statements and (ii) MD&A.

#### (c) DESCRIPTION OF BUSINESS

Kemper is a diversified insurance holding company, with subsidiaries that provide automobile, homeowners, life, health, and other insurance products to individuals and businesses. The Company is engaged, through its subsidiaries, in the property and casualty insurance and life and health insurance businesses. The Company conducts its operations through two operating segments: Property & Casualty Insurance and Life & Health Insurance. The Company's operations are conducted solely in the United States.

Kemper's subsidiaries employ approximately 5,350 full-time associates supporting their operations, of which approximately 1,450 are employed in the Property & Casualty Insurance segment, approximately 3,500 are employed in the Life & Health Insurance segment and the remainder are employed in various corporate and other staff and shared functions.

## Property and Casualty Insurance Business

## General

The Property & Casualty Insurance segment mostly distributes its products through independent agents and brokers who are paid commissions for their services. The Property & Casualty Insurance segment's products are also distributed through employer-sponsored voluntary benefit programs and other affinity relationships. The Property & Casualty Insurance segment's direct-to-consumer operations were placed into run-off in 2012 and accounted for approximately 8% of the Property & Casualty Insurance segment's earned premiums in 2014. The Property & Casualty Insurance segment provides automobile, homeowners, renters, fire, umbrella and other types of property and casualty insurance to individuals and commercial automobile insurance to businesses. In addition, the Life & Health Insurance segment's career agents also sell contents coverage for personal property to its customers.

Property insurance indemnifies an insured with an interest in physical property for loss of, or damage to, such property. Casualty insurance primarily covers liability for damage to property of, or injury to, a person or entity other than the insured. In most cases, casualty insurance also obligates the insurance company to provide a defense for the insured in litigation arising out of events covered by the policy.

Earned premiums from automobile insurance accounted for 48%, 50% and 52% of the Company's consolidated insurance premiums earned in 2014, 2013 and 2012, respectively. Revenues from automobile insurance accounted for 43%, 44% and 47% of Kemper's consolidated revenues from continuing operations in 2014, 2013 and 2012, respectively. Automobile insurance products include personal automobile insurance, ranging from preferred and standard risk to nonstandard risks, and commercial automobile insurance. Nonstandard personal automobile insurance policyholders tend to have difficulty obtaining standard or preferred risk insurance, usually because of their driving records, claims experience or premium payment history. Homeowners insurance accounted for 17%, 16% and 15% of the Company's consolidated insurance premiums earned in 2014, 2013 and 2012, respectively. Homeowners insurance accounted for 15%, 14% and 14% of the Company's consolidated revenues from continuing operations in 2014, 2013 and 2012, respectively.

The Property & Casualty Insurance segment is headquartered in Chicago, Illinois, and conducts business in 47 states and the District of Columbia. The segment's insurance products are offered by approximately 15,300 independent insurance agents and brokers. As shown in the following table, five states provided 62% of the segment's premium revenues in 2014.

State	Percentage of Total Premiums
California	22 %
Texas	14
New York	14
North Carolina	8
Washington	4



## Property and Casualty Loss and Loss Adjustment Expense Reserves

The Company's reserves for losses and LAE for property and casualty insurance ("Property and Casualty Insurance Reserves") are reported using the Company's estimate of its ultimate liability for losses and LAE for claims that occurred prior to the end of any given accounting period but have not yet been paid.

Property and Casualty Insurance Reserves by business segment at December 31, 2014 and 2013 were:

DOLLARS IN MILLIONS	2014	2013
Business Segments:		
Property & Casualty Insurance	\$651.1	\$742.6
Life & Health Insurance	4.5	5.3
Total Business Segments	655.6	747.9
Discontinued Operations	70.2	83.0
Unallocated Reserves	8.1	12.6
Total Property and Casualty Insurance Reserves	\$733.9	\$843.5

In estimating the Company's Property and Casualty Insurance Reserves, the Company's actuaries exercise professional judgment and must consider, and are influenced by, many variables that are difficult to quantify. Accordingly, the process of estimating and establishing the Company's Property and Casualty Insurance Reserves is inherently uncertain and the actual ultimate net cost of claims may vary materially from the estimated amounts reserved. The reserving process is particularly imprecise for claims involving asbestos, environmental matters, construction defect and other emerging and/or long-tailed exposures that may not be discovered or reported until years after the insurance policy period has ended. Property and Casualty Insurance Reserves related to the Company's Discontinued Operations are predominantly long-tailed exposures, of which \$28.4 million was related to asbestos, environmental matters and construction defect exposures at December 31, 2014. See MD&A, "Critical Accounting Estimates," under the caption "Property and Casualty Insurance Reserves for Losses and Loss Adjustment Expenses" beginning on page 53 for a discussion of the Company's reserving process and the factors considered by the Company's actuaries in estimating the Company's Property and Casualty Insurance Reserves.

The Company's goal is to ensure that its total reserves for property and casualty insurance losses and LAE are adequate to cover all costs, while minimizing variation from the time reserves for losses and LAE are initially estimated until losses and LAE are fully developed. Changes in the Company's estimates of these losses and LAE, also referred to as "development," will occur over time and may be material. Favorable development is recognized and reported in the Consolidated Financial Statements when the Company decreases its previous estimate of ultimate losses and LAE and results in an increase in net income in the period recognized, whereas adverse development is recognized and reported in the Consolidated Financial Statements when the Company increases its previous estimate of ultimate losses and LAE and results in a decrease in net income.

Development of property and casualty insurance losses and LAE from prior accident years for each of the Company's continuing business segments and discontinued operations in 2014, 2013 and 2012 was:

DOLLARS IN MILLIONS	Favorable (Adverse) Development		
	2014	2013	2012
Continuing Operations:			
Property & Casualty Insurance	\$54.4	\$58.0	\$24.9
Life & Health Insurance	(0.9)	1.8	0.3
Total Favorable Development from Continuing Operations, Net	53.5	59.8	25.2
Discontinued Operations	3.6	4.8	6.3
Total Favorable Development, Net	\$57.1	\$64.6	\$31.5

See MD&A, "Loss and LAE Reserve Development," "Property & Casualty Insurance," and "Life & Health Insurance," for the impact of development on the results reported by the Company's business segments. Also see MD&A, "Critical Accounting Estimates," under the caption "Property and Casualty Insurance Reserves for Losses and Loss Adjustment Expenses" beginning on page 53 for additional information about the Company's reserving practices.

See Note 5, "Property and Casualty Insurance Reserves," to the Consolidated Financial Statements for a tabular reconciliation of the three most recent annual periods setting forth the Company's Property and Casualty Insurance Reserves as of the beginning of each year, incurred losses and LAE for insured events of the current year, changes in

incurred losses and LAE for

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insured events of prior years, payments of losses and LAE for insured events of the current year, payments of losses and LAE for insured events of prior years and the Company's Property and Casualty Insurance Reserves at the end of the year and additional information regarding the nature of adjustments to incurred losses and LAE for insured events of prior years.

#### Catastrophe Losses

Catastrophes and natural disasters are inherent risks of the property and casualty insurance business. These catastrophic events and natural disasters include, without limitation, hurricanes, tornadoes, earthquakes, hailstorms, wildfires, high winds and winter storms. Such events result in insured losses that are, and are expected to be, a material factor in the results of operations and financial position of Kemper's property and casualty insurance companies. Further, because the level of insured losses that could occur in any one year cannot be accurately predicted, these losses contribute to material year-to-year fluctuations in the results of operations and financial position of these companies. Specific types of catastrophic events are more likely to occur at certain times within the year than others. This factor adds an element of seasonality to property and casualty insurance claims. The occurrence and severity of catastrophic events cannot be accurately predicted in any year. However, some geographic locations are more susceptible to these events than others. The Company has endeavored to manage its direct insurance exposures in certain regions that are prone to naturally occurring catastrophic events through a combination of geographic diversification, restrictions on the amount and location of new business production in such regions, and reinsurance. The Company has adopted the industry-wide catastrophe classifications of storms and other events promulgated by Insurance Services Office, Inc. ("ISO") to track and report losses related to catastrophes. ISO classifies a disaster as a catastrophe when the event causes \$25 million or more in direct insured losses to property and affects a significant number of policyholders and insurers. ISO-classified catastrophes are assigned a unique serial number recognized throughout the insurance industry. The discussions throughout this 2014 Annual Report utilize ISO's definition of catastrophes.

The process of estimating and establishing reserves for catastrophe losses is inherently uncertain and the actual ultimate cost of a claim, net of reinsurance recoveries, may vary materially from the estimated amount reserved. See Item 1A., "Risk Factors," under the caption "Catastrophe losses could materially and adversely affect the Company's results of operations, liquidity and/or financial condition, the availability of reinsurance and the ratings of Kemper and its insurance subsidiaries" for a discussion of catastrophe risk. See Note 19, "Catastrophe Reinsurance," to the Consolidated Financial Statements for a discussion of the factors that influence the process of estimating and establishing reserves for catastrophes.

#### Reinsurance

The Company manages its exposure to catastrophes and other natural disasters through a combination of geographical diversification, restrictions on the amount and location of risks insured in certain regions and reinsurance. To limit its exposures to catastrophic events, the Company maintains a primary catastrophe reinsurance program for the Property & Casualty Insurance segment. Coverage for the primary catastrophe reinsurance program is provided in various layers. The Property & Casualty Insurance segment and the Life & Health Insurance segment also purchase reinsurance from the Florida Hurricane Catastrophe Fund (the "FHCF") for hurricane losses in Florida at retentions lower than those described below for the Company's primary catastrophe reinsurance program.

Effective January 1, 2015, the Property & Casualty Insurance segment's primary catastrophe reinsurance program provides coverage over the three-year period of January 1, 2015 through December 31, 2017. Coverage provided under the program for the first year (January 1, 2015 to December 31, 2015) is provided in various layers as presented below.

DOLLARS IN MILLIONS	Catastrophe Losses and LAE		Percentage of Coverage	
	In Excess of	Up to		%
Retained	\$—	\$50.0	—	
1st Layer of Coverage	50.0	150.0	95.0	
2nd Layer of Coverage	150.0	350.0	95.0	

Under the reinsurance contract, the participation of each reinsurer, decreases by one-third in the second year and another one-third in the third year. Accordingly, the percentage of coverage in the second and third years is 63.3% and

31.7%, respectively, and, to maintain the same percentage of coverage as provided in the first year, the Property & Casualty Insurance segment will need to purchase additional reinsurance for the second and third years. The estimated aggregate annual premium in 2015 for the program presented in the preceding table is \$14.5 million for the Property & Casualty Insurance segment's catastrophe reinsurance program. Premiums due to the reinsurers will decrease proportionately with the decline in their respective participations in the second and third years. In the event that the Company's incurred catastrophe losses and LAE covered by its catastrophe reinsurance program exceed the retention for a particular layer, the program requires one reinstatement of such

coverage. In such an instance, the Company is required to pay a reinstatement premium to the reinsurers to reinstate the full amount of reinsurance available under such layer. The reinstatement premium is a percentage of the original premium based on the ratio of the losses in excess of the Company's retention to the reinsurers' coverage limit. The coverage presented in the preceding table differs from the coverage provided in 2014, 2013 and 2012. See Note 19, "Catastrophe Reinsurance," to the Consolidated Financial Statements for information pertaining to the primary catastrophe reinsurance programs for the Property & Casualty Insurance segment for 2014, 2013 and 2012. Prior to 2013, companies operating in the Life & Health Insurance segment participated in a catastrophe reinsurance program separate and apart from the catastrophe reinsurance programs covering the Property & Casualty Insurance segment. Over the last several years, the Life & Health Insurance segment has been reducing its exposure to catastrophic events through the intentional run-off of its dwelling insurance business. Accordingly, the Life & Health Insurance segment did not renew its catastrophe reinsurance program for 2013. See Note 19, "Catastrophe Reinsurance," to the Consolidated Financial Statements for information pertaining to the Life & Health Insurance segment's participation in the Company's catastrophe reinsurance programs for 2012.

In addition to the catastrophe loss exposures caused by natural events described above, Kemper's property and casualty insurance companies are exposed to losses from catastrophic events that are not the result of acts of nature, such as acts of terrorism, the nature, occurrence and severity of which in any period cannot be accurately predicted. The companies have reinsurance coverage to address certain exposures to potential future terrorist attacks. The reinsurance coverage for certified events, as designated by the federal government, is from the Terrorist Risk Insurance Act and the coverage for non-certified events is available in the catastrophe reinsurance program for Kemper's Property & Casualty Insurance segment. However, certain perils, such as biological, chemical, nuclear pollution or contamination, are excluded from the reinsurance coverage for non-certified events.

In addition to the catastrophe reinsurance programs described above, Kemper's property and casualty insurance companies utilize other reinsurance arrangements to limit their maximum loss, provide greater diversification of risk and minimize exposures on larger risks.

Under the various reinsurance arrangements, Kemper's property and casualty insurance companies are indemnified by reinsurers for certain losses incurred under insurance policies issued by the reinsurers. As indemnity reinsurance does not discharge an insurer from its direct obligations to policyholders on risks insured, Kemper's property and casualty insurance companies remain directly liable. However, provided that the reinsurers meet their obligations, the net liability for Kemper's property and casualty insurance companies is limited to the amount of risk that they retain. Kemper's property and casualty insurance companies purchase their reinsurance only from reinsurers rated "A-" or better by A. M. Best Co., Inc. ("A.M. Best"), at the time of purchase. A.M. Best is an organization that specializes in rating insurance and reinsurance companies.

For further discussion of the reinsurance programs, see Note 19, "Catastrophe Reinsurance," and Note 20, "Other Reinsurance," to the Consolidated Financial Statements.

#### Pricing

Pricing levels for property and casualty insurance are influenced by many factors, including the frequency and severity of claims, state regulation and legislation, competition, general business and economic conditions, including market rates of interest, inflation, expense levels, and judicial decisions. In addition, many state regulators require consideration of investment income when approving or setting rates, which could reduce underwriting margins. See MD&A under the caption "Property & Casualty Insurance."

#### Competition

Based on the most recent annual data published by A.M. Best, as of the end of 2013, there were 1,266 property and casualty insurance groups in the United States. Kemper's property and casualty group was among the top 10% of property and casualty insurance groups in the United States as measured by net written premiums, policyholders' surplus and admitted assets in 2013. Among all personal lines automobile insurance writers, Kemper's property and casualty group was the 24th largest writer as measured by net written premiums in 2013.

Rankings by admitted assets, net premiums written and capital and surplus were:

Measurement	Ordinal Rank	Percentile Rank	
Net Admitted Assets	121	90	%
Net Written Premiums	64	94	
Capital and Surplus	125	90	

In 2013, the property and casualty insurance industry's estimated net premiums written were \$487 billion, of which nearly 60% were accounted for by the top 50 groups of property and casualty insurance companies. Kemper's property and casualty insurance companies wrote less than 1% of the industry's 2013 premium volume.

The property and casualty insurance industry is highly competitive, particularly with respect to personal automobile insurance. Kemper's property and casualty insurance companies compete on the basis of, among other measures, (i) using suitable pricing segmentation, (ii) maintaining underwriting discipline, (iii) offering products in selected markets or geographies, (iv) utilizing technological innovations for the marketing and sale of insurance, (v) controlling expenses, (vi) maintaining adequate ratings from A.M. Best and other ratings agencies and (vii) providing quality services to independent agents and policyholders. See Item 1A., "Risk Factors," under the caption "The insurance industry is highly competitive."

#### Life and Health Insurance Business

The Company's Life & Health Insurance segment consists of Kemper's wholly-owned subsidiaries, United Insurance Company of America ("United Insurance"), The Reliable Life Insurance Company ("Reliable"), Union National Life Insurance Company ("Union National Life"), Mutual Savings Life Insurance Company ("Mutual Savings Life"), United Casualty Insurance Company of America ("United Casualty"), Union National Fire Insurance Company ("Union National Fire"), Mutual Savings Fire Insurance Company ("Mutual Savings Fire") and Reserve National Insurance Company ("Reserve National"). As discussed below, United Insurance, Reliable, Union National Life, Mutual Savings Life, United Casualty, Union National Fire and Mutual Savings Fire (the "Kemper Home Service Companies") distribute their products through a network of employee, or "career," agents. Reserve National distributes its products through a network of independent agents and brokers. These career agents, independent agents and brokers are paid commissions for their services.

Earned premiums from life insurance accounted for 21%, 19% and 19% of the Company's consolidated insurance premiums earned in 2014, 2013 and 2012, respectively. Revenues from life insurance accounted for 27%, 24% and 24% of the Company's consolidated revenues from continuing operations in 2014, 2013 and 2012, respectively. As shown in the following table, five states provided 51% of the premium revenues in this segment in 2014.

State	Percentage of Total Premiums	
Texas	21	%
Louisiana	12	
Alabama	7	
Mississippi	6	
Florida	5	

#### Kemper Home Service Companies

The Kemper Home Service Companies, based in St. Louis, Missouri, focus on providing individual life and supplemental accident and health insurance products to customers of modest incomes who desire basic protection for themselves and their families. Their leading product is ordinary life insurance, including permanent and term insurance. Face amounts of these policies are lower than those of policies typically sold to higher income customers by other companies in the life insurance industry. Approximately 78% of the Life & Health Insurance segment's premium revenues are generated by the Kemper Home Service Companies.

The Kemper Home Service Companies employ nearly 2,400 career agents to distribute insurance products in 25 states and the District of Columbia. These career agents are full-time employees who call on customers in their homes to sell insurance products, provide services related to policies in force and collect premiums, typically monthly. Premiums average about \$19 per policy per month with an average face value of \$5,300. Permanent and term policies are offered

primarily on a non-

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participating, guaranteed-cost basis. These career agents also distribute and/or service certain property insurance products for the Kemper Home Service Companies.

#### Reserve National

Reserve National, based in Oklahoma City, Oklahoma, is licensed in 48 states throughout the United States and has traditionally specialized in the sale of Medicare Supplement insurance and limited health insurance coverages such as fixed indemnity and accident-only plans, primarily to individuals in rural areas who often do not have access to a broad array of accident and health insurance products tailored to meet their individual and family needs. There are approximately 300 independent agents that primarily represent Reserve National.

Reserve National began expanding its distribution channels during 2013 by launching two marketing channel initiatives —Kemper Senior Solutions and Kemper Benefits. Kemper Senior Solutions markets life insurance and home health care products focusing on the individual, senior-age demographic of the market place. Kemper Benefits sells voluntary products in the employer market place. Brokers and non-exclusive independent agents are utilized to market and distribute products in these new distribution channels. Reserve National has appointed approximately 20,000 independent agents in connection with these initiatives.

See “Regulation,” under this Item 1 beginning on page 10, Item 1A., “Risk Factors,” under the caption “Reserve National’s operating history with its expanded distribution channels and new products is limited,” and MD&A, “Life & Health Insurance,” for a discussion of the impact of the Health Care Acts on Reserve National.

#### Reinsurance

Consistent with insurance industry practice, the Company’s life and health insurance companies utilize reinsurance arrangements to limit their maximum loss, provide greater diversification of risk and minimize exposures on larger risks. Prior to 2013, the Life & Health Insurance segment’s reinsurance arrangements included excess of loss reinsurance coverage specifically designed to protect against losses arising from catastrophic events under the property insurance policies distributed by the Kemper Home Service Companies’ agents and written by Kemper’s subsidiaries, United Casualty, Union National Fire and Mutual Savings Fire, and reinsured by Kemper’s subsidiary, Trinity Universal Insurance Company (“Trinity”), or written by Capitol County Mutual Fire Insurance Company (“Capitol”), a mutual insurance company owned by its policyholders, and its subsidiary, Old Reliable Casualty Company (“ORCC”), and reinsured by Trinity. Over the last several years, the segment has been intentionally reducing its exposure to catastrophic events through the run-off of its dwelling insurance business. Accordingly, except for catastrophe reinsurance provided by the FHCF, the Kemper Home Service Companies, Capitol and ORCC did not carry catastrophe reinsurance in 2014 and 2013. The FHCF provides reinsurance for catastrophe losses in Florida. See Note 19, “Catastrophe Reinsurance,” to the Consolidated Financial Statements for additional information pertaining to the segment’s primary catastrophe reinsurance programs for 2012.

#### Lapse Ratio

The lapse ratio is a measure of a life insurer’s loss of in-force policies. For a given year, this ratio is commonly computed as the total face amount of individual life insurance policies lapsed, surrendered, expired and decreased during such year, less policies increased and revived during such year, divided by the total face amount of policies at the beginning of the year plus the face amount of policies issued and reinsurance assumed in the prior year. The Life & Health Insurance segment’s lapse ratio for individual life insurance was 7%, 7% and 8% in 2014, 2013 and 2012, respectively.

The customer base served by the Kemper Home Service Companies and competing life insurance companies tends to have a higher incidence of lapse than other demographic segments of the population. Thus, to maintain or increase the level of its business, the Kemper Home Service Companies must write a high volume of new policies.

#### Pricing

Premiums for life and health insurance products are based on assumptions with respect to mortality, morbidity, investment yields, expenses, and lapses and are also affected by state laws and regulations, as well as competition. Pricing assumptions are based on the experience of Kemper’s life and health insurance subsidiaries, as well as the industry in general, depending on the factor being considered. The actual profit or loss produced by a product will vary from the anticipated profit if the actual experience differs from the assumptions used in pricing the product.





Premiums for policies sold by the Kemper Home Service Companies are set at levels designed to cover the relatively high cost of “in-home” servicing of such policies. As a result of such higher expenses, incurred claims as a percentage of earned premiums tend to be lower for companies utilizing this method of distribution than the life insurance industry average.

Premiums for Medicare supplement and other accident and health policies must take into account the rising costs of medical care. The annual rate of medical cost inflation has historically been higher than the general rate of inflation, necessitating frequent rate increases, most of which are subject to approval by state regulators.

#### Competition

Based on the most recent data published by A.M. Best, as of the end of 2013, there were 442 life and health insurance company groups in the United States. The Company’s Life & Health Insurance segment ranked in the top 21% of life and health insurance company groups, as measured by admitted assets, net premiums written and capital and surplus. Rankings by admitted assets, net premiums written and capital and surplus were:

Measurement	Ordinal Rank	Percentile Rank	
Net Admitted Assets	88	80	%
Net Written Premiums	88	80	
Capital and Surplus	93	79	

Kemper’s life and health insurance subsidiaries generally compete by using appropriate pricing, offering products to selected markets or geographies, controlling expenses, maintaining adequate ratings from A.M. Best and providing competitive services to agents and policyholders.

#### Investments

The quality, nature and amount of the various types of investments that can be made by insurance companies are regulated by state laws. Depending on the state, these laws permit investments in qualified assets, including, but not limited to, municipal, state and federal government obligations, corporate bonds, real estate, preferred and common stocks, investment partnerships, and limited liability investment companies and limited partnerships. In addition, the quality, nature and amount of the various types of investments held by Kemper’s insurance subsidiaries affect the amount of asset risk calculated by regulators and rating agencies in determining required capital. See “Regulation” immediately following this subsection of Item 1 and Item 1A., “Risk Factors,” under the caption “The Company’s investment portfolio is exposed to a variety of risks that may negatively impact net investment income and cause realized and unrealized losses.”

The Company employs a total return investment strategy, with an emphasis on yield, while maintaining liquidity to meet both its short- and long-term insurance obligations. See the discussions of the Company’s investments under the headings “Investment Results,” “Investment Quality and Concentrations,” “Investments in Limited Liability Companies and Limited Partnerships,” “Liquidity and Capital Resources” and “Critical Accounting Estimates,” in the MD&A, “Quantitative and Qualitative Disclosures about Market Risk,” in Item 7A and Note 3, “Investments,” Note 12, “Income from Investments,” and Note 21, “Fair Value Measurements,” to the Consolidated Financial Statements.

#### Regulation

##### Insurance Regulation

Kemper’s insurance subsidiaries are subject to extensive regulation in the states in which they conduct business. Such regulation pertains to a variety of matters, including, but not limited to, policy forms, premium rate plans, licensing of agents, licenses to transact business, market conduct, trade practices, claims practices, investments and solvency. The majority of Kemper’s insurance operations are in states requiring prior approval by regulators before proposed rates for property, casualty, or health insurance policies may be implemented. However, provided that the policy form has been previously approved, rates proposed for life insurance generally become effective immediately upon filing with a state, even though the same state may require prior rate approval for other types of insurance. Insurance regulatory authorities perform periodic examinations of an insurer’s market conduct and other affairs. Kemper’s health insurance subsidiaries are also subject to certain regulation by the federal government. For example, the Health Care Acts, and the regulations promulgated thereunder, have established minimum loss ratios, rating restrictions, mandates for essential health benefit coverages, and restrictions or prohibitions on pre-existing condition exclusions and annual and lifetime policy limits for health insurance policies.



Insurance companies are required to report their financial condition and results of operation in accordance with statutory accounting principles prescribed or permitted by state insurance regulators in conjunction with the National Association of Insurance Commissioners (the "NAIC"). State insurance regulators also prescribe the form and content of statutory financial statements, perform periodic financial examinations of insurers, set minimum reserve and loss ratio requirements and establish standards for the types and amounts of investments. In addition, state regulators require minimum capital and surplus levels and incorporate risk-based capital ("RBC") standards promulgated by the NAIC. These RBC standards are intended to assess the level of risk inherent in an insurance company's business and consider items such as asset risk, credit risk, underwriting risk and other business risks relevant to its operations. In accordance with RBC formulas, a company's RBC requirements are calculated and compared to its total adjusted capital to determine whether regulatory intervention is warranted. At December 31, 2014, the total adjusted capital of each of Kemper's insurance subsidiaries exceeded the minimum levels required under applicable RBC rules.

Kemper's insurance subsidiaries are required to pay assessments up to prescribed limits to fund policyholder losses or liabilities of insolvent insurance companies under the guaranty fund laws of most states in which they transact business. Kemper's insurance subsidiaries are subject to certain fees imposed on health insurers by the Health Care Acts, including the Health Insurance Providers Fee, but not the fees associated with the Reinsurance, Risk Adjustment and Risk Corridor programs, as Kemper's insurance subsidiaries do not have any policies subject to those fees.

Kemper's insurance subsidiaries are also required to participate in various involuntary pools or assigned risk pools, principally involving windstorms and high risk drivers. In most states, the involuntary pool participation of Kemper's insurance subsidiaries is set in proportion to their voluntary writings of related lines of business in such states. See Item 1A., "Risk Factors," under the caption "Catastrophe losses could materially and adversely affect the Company's results of operations, liquidity and/or financial condition, the availability of reinsurance and the ratings of Kemper and its insurance subsidiaries" for a discussion of the impact of required participation in windstorm pools and joint underwriting associations on the ability of the Company to manage its exposure to catastrophic events.

Kemper and its insurance subsidiaries are also subject to the insurance holding company laws of a number of states. Certain dividends and distributions by an insurance subsidiary are subject to prior approval by the insurance regulators of its state of domicile. See Item 1A., "Risk Factors," under the caption "Kemper relies on receiving dividends from its subsidiaries to service its debt, to pay dividends to its shareholders or make repurchases of its stock." Other significant transactions between an insurance subsidiary and its holding company or other affiliates may require approval by insurance regulators in the state of domicile of each participating insurance subsidiary. A number of pending and recently approved legislative and regulatory measures may significantly affect the insurance business. In particular, nearly half of all states have already adopted extensive modifications to their holding company laws based on amendments to the Model Insurance Holding Company System Regulatory Act ("IHCS") adopted by the NAIC in December 2010. With varying effective dates beginning in 2014, these modifications impose new reporting requirements and substantially expand the oversight and examination powers of state insurance regulators with regulatory authority over an insurance company to assess enterprise risks within such company's entire holding company system that may arise from operations of its insurance and non-insurance affiliates. They also impose new reporting requirements on the ultimate controlling persons of such insurance companies in respect of, among other things, affiliated transactions and divestiture of controlling interests in the insurance companies. In addition, a number of states have adopted RMORSA adopted by the NAIC in September 2012. With varying effective dates beginning in 2015, RMORSA requires insurers to maintain an enterprise risk management ("ERM") framework, perform regular assessments of the adequacy of the ERM framework and the company's solvency and file an annual ERM assessment summary report. Similarly, in late 2014, the NAIC adopted the Corporate Governance Annual Disclosure Model Act ("CGADM") and Model Regulation. The CGADM has an effective date of June 1, 2016, and when adopted by a state, requires an insurer (or insurance group) to submit a Corporate Governance Annual Disclosure to its lead state or domestic regulator to provide, among other things, information about board structure and policies, meeting frequency, procedures for the oversight of critical risk areas and practices, and policies and practices used by the board of directors for directing senior management in critical areas such as codes of business conduct and ethics and governance processes. The Company anticipates that most states will adopt legislation based on IHCS, RMORSA and CGADM. Additional regulation has also resulted from other measures in recent years including, among other things, tort reform, the Health Care Acts, the DFA, consumer privacy and data security requirements, credit score regulation,

producer compensation regulations, cyber security and financial services regulation initiatives. State insurance laws also impose requirements that must be met prior to a change of control of an insurance company or insurance holding company based on the insurer's state of domicile and, in some cases, additional states in which it is deemed commercially domiciled due to the substantial amount of business it conducts therein. These requirements may include the advance filing of specific information with the state insurance regulators, a public hearing on the matter, and the review and approval of the change of control by such regulators. The Company has insurance subsidiaries domiciled or deemed commercially domiciled in Alabama, California, Illinois, Louisiana, Missouri, New York, Oklahoma, Oregon, Texas and

Wisconsin. In these states, except Alabama, “control” generally is presumed to exist through the direct or indirect ownership of 10% or more of the voting securities of an insurance company. Control is presumed to exist in Alabama with a 5% or more ownership interest in such securities. Any purchase of Kemper’s shares that would result in the purchaser owning Kemper’s voting securities in the foregoing percentages for the states indicated would be presumed to result in the acquisition of control of Kemper’s insurance subsidiaries in those states. Therefore, acquisitions subject to the 10% threshold generally would require the prior approval of insurance regulators in each state in which Kemper’s insurance subsidiaries are domiciled or deemed commercially domiciled, including those in Alabama, while acquisitions subject to the 5% threshold generally would require the prior approval of only Alabama regulators. Similarly, consistent with the IHCS, several states have enacted legislation that requires either the acquiring and/or divesting company to notify and receive regulatory approval for a change in control. Other states are expected to adopt similar provisions.

Many state statutes also require pre-acquisition notification to state insurance regulators of a change of control of an insurance company licensed in the state if specific market concentration thresholds would be triggered by the acquisition. Such statutes authorize the issuance of a cease and desist order with respect to the insurance company if certain conditions, such as undue market concentration, would result from the acquisition. These regulatory requirements may deter, delay or prevent transactions effecting control of Kemper or its insurance subsidiaries, or the ownership of Kemper’s voting securities, including transactions that could be advantageous to Kemper’s shareholders.

#### Dodd-Frank Act

The DFA, enacted in July 2010, profoundly increases federal regulation of the financial services industry, of which the insurance industry is a part. Among other things, the DFA formed a Federal Insurance Office (“FIO”) charged with monitoring the insurance industry and conducting a study on methods to modernize and improve the insurance regulatory system in the United States. FIO’s report, delivered to Congress in December 2013, concluded that a hybrid approach to regulation, involving a combination of state and federal government action, could improve the U.S. insurance system by attaining uniformity, efficiency and consistency, particularly with respect to solvency and market conduct regulation. A hybrid approach was also recommended to address the perceived need for uniform supervision of insurance companies with national and global activities. FIO recently established the Federal Advisory Committee on Insurance (“FACI”) whose mission is to provide recommendations to FIO on issues it monitors for Congress. While the NAIC continues to promote the strengths of the U.S. state-based insurance regulatory system, both FIO/FACI and international standard setting authorities such as the International Association of Insurance Supervisors are actively seeking a role in shaping the future of the U.S. insurance regulatory framework. It is too early to know whether or how these organizations’ recommendations might result in changes to the current state-based system of insurance industry regulation or ultimately impact Kemper’s operations.

#### Item 1A. Risk Factors.

Kemper is exposed to numerous risk factors that could cause actual results to differ materially from recent results or anticipated future results. The following discussion details the significant risk factors that are specific to the Company. In addition to those described below, the Company’s business, financial condition and results of operations could be materially affected by other factors not presently known by, or considered material to, the Company. Readers are advised to consider all of these factors along with the other information included in this 2014 Annual Report, and to consult any further disclosures Kemper makes on related subjects in its filings with the SEC.

Changes in the application of state unclaimed property laws and related insurance claims handling practices, particularly attempts by state officials to apply such changes retroactively to existing insurance policies through new laws and regulations, examinations and audits, could result in new requirements that would have a significant effect on (including an acceleration of) the payment and/or escheatment of life insurance death benefits and significantly increase claims handling costs relative to what is currently contemplated by Kemper. If attempts by state officials to impose such new requirements on existing insurance policies are successful on a wide scale, there is a potential for their collective effects to be materially adverse to the Company’s profitability, financial position and cash flows (the “Unclaimed Property Risk Factor”).

In recent years, many states have begun to aggressively expand the application of their unclaimed property laws as they relate to life insurance proceeds. The treasurers or controllers (collectively, “Treasurers”) of a large majority of states have engaged private audit firms to examine the practices and procedures of life insurance companies with

respect to the reporting and remittance of proceeds associated with life insurance policies, annuity contracts and retained asset accounts under state unclaimed property laws. Certain related measures are also being taken or considered by state insurance regulators, both individually and collectively through the auspices of the NAIC. Some state insurance regulators have initiated market conduct examinations focused on claims handling and escheatment practices of life insurance companies.

As a result of these audits and examinations, a number of large life insurance companies have agreed to alter historic practices that were previously considered to be lawful and appropriate relative to claims handling and the reporting and remittance of life insurance policy proceeds to the states under state unclaimed property laws. Based on published reports, at least sixteen life insurance companies have entered into settlement agreements with state insurance regulators and twenty-one with Treasurers. Under the terms of these agreements, the settling insurance companies typically have agreed to establish a practice of periodically searching for deceased insureds, even prior to the receipt of a death claim, by comparing their in-force policy records against a database of reported deaths maintained by the Social Security Administration or a comparable database (collectively, a “Death Master File” or “DMF”). The settlements typically apply to policies that were in force at any time since January 1, 1992. In conducting these data comparisons against a Death Master File, the insurers are required to use complex “fuzzy” matching criteria which in many cases result in numerous potential matches for any given insured. In such cases, the insurer must either assume a costly and administratively burdensome process of disproving any such ambiguous matches which may, in some cases, necessitate a review of older records that are not in electronic form or accept such matches as valid and escheat the related policy benefits to the states if the beneficiaries cannot be found. All settlements to date with insurance regulators have involved payment of monetary penalties (involving amounts ranging from about \$1.2 million up to \$40 million), while settlements with Treasurers have required payment of interest on sums remitted to the Treasurers dating from the date of death of the insured (rather than from a more recent date linked to the insurer’s first awareness of death) and extending as far back as January 1, 1995. As hereafter described, Kemper’s life insurance subsidiaries (the “Life Companies”) have thus far resisted attempts by certain state officials and their agents to mandate changes to the Life Companies’ claims handling and escheatment practices of the sort embodied in the foregoing settlements and have challenged through legal proceedings the authority of such officials to require such changes. There can be no assurances that the Life Companies will ultimately be successful in resisting such attempts or any that may arise in the future.

Separately, the National Conference of Insurance Legislators (“NCOIL”) has adopted model legislation which, if enacted by states as proposed, would require life insurance companies to compare their in-force life insurance policy records against a Death Master File for the purpose of proactively identifying potentially deceased insureds for whom the subject life insurance company has not yet received a claim, including due proof of death. Ten states have enacted legislation of this type, with varying effective dates (the “DMF Statutes”). Such statutes, if construed to apply to life insurance policies in force on each respective statute’s effective date, could have a significant effect on, including an acceleration of, the payment of life insurance benefits to beneficiaries or, in instances where beneficiaries could not be located, the remittance of such benefits to the states under their unclaimed property laws. In contrast, New Mexico and Tennessee have enacted a version of the model legislation that applies only prospectively to life insurance companies, like Kemper’s Life Companies, that have not previously used a Death Master File. Similarly, Georgia, Mississippi and Alabama have enacted statutes that apply only to policies issued on or after their respective effective dates, without regard to prior Death Master File use. Various forms of DMF legislation are pending in several states, and Kemper believes that it is likely that a number of other states will introduce (or re-introduce) legislation of this sort in 2015. Kemper cannot presently predict whether any of such pending or future legislation will be enacted or, if enacted, exactly what form such legislation will take.

In November 2012, certain of the Life Companies filed a declaratory judgment action in Kentucky state court challenging the Kentucky DMF Statute on statutory and constitutional grounds, insofar as it purports to impose new requirements with respect to existing, previously issued life insurance policies. The trial court in that case denied the subject Life Companies’ motion for summary judgment and held that the requirements of the Kentucky DMF Statute apply to life insurance policies issued before the Kentucky DMF Statute’s January 1, 2013 effective date. The Life Companies appealed the trial court decision to the Kentucky Court of Appeals, and in August 2014, in a unanimous opinion, the Kentucky Court of Appeals reversed the trial court and held that the Kentucky DMF statute fell within Kentucky’s statutory presumption against retroactivity. As a result, the Court ruled, the Kentucky DMF Statute can only apply to policies issued on and after January 1, 2013. In September 2014, the Kentucky Department of Insurance filed a motion asking for the Kentucky Supreme Court to undertake a discretionary review of the Court of Appeals’ ruling. A decision by the Kentucky Supreme Court on whether to review the Court of Appeals’ decision is expected by the third quarter of 2015.



In July 2013, certain of the Life Companies filed a declaratory judgment action, similar to the Kentucky action, in Maryland state court asking the court to construe the Maryland DMF Statute to apply only prospectively, i.e., only with respect to those life insurance policies issued in Maryland on or after the effective date of the Maryland DMF Statute, consistent with what the Life Companies believe are the requirements of the Maryland Constitution and the Contract Clause of the United States Constitution. The Maryland Insurance Administration filed a motion to dismiss the action on jurisdictional grounds, contending that the Life Companies failed to first exhaust their administrative remedies before filing their action in the trial court. In March 2014, the trial court granted the Maryland Insurance Administration's motion. The Life Companies appealed the trial court's ruling to the Maryland Court of Special Appeals. The Maryland appellate courts have declined to stay enforcement of the Maryland DMF Statute pending the appeal, and the Life Companies are complying with the Maryland DMF Statute while they

continue to pursue their appeal. The Life Companies' appeal was heard by the Maryland Court of Special Appeals in December 2014. The parties are awaiting the court's decision.

In August 2014, certain of the Life Companies filed a declaratory judgment action in Indiana state court, asking the court to construe the Indiana DMF Statute to apply only prospectively, i.e., only with respect to those life insurance policies issued in Indiana on or after the effective date of the Indiana DMF Statute, consistent with what the Life Companies believe are the requirements of applicable Indiana statutory law, the Indiana Constitution and the Contract Clause of the United States Constitution. The Indiana Department of Insurance filed an answer in response to the subject Life Companies' complaint in October 2014, and the Life Companies filed a motion for summary judgment in January 2015. A hearing on that motion is scheduled for May 2015.

The Life Companies are the subject of an unclaimed property compliance audit (the "Treasurers' Audit") by a private audit firm retained by the Treasurers of 38 states (the "Audit Firm"). In July 2013, the California State Controller (the "CA Controller") filed a complaint for injunctive relief against the Life Companies in state court in California, seeking an order requiring the Life Companies to produce all of their in-force insurance policy records to the Audit Firm to enable the firm to perform a comparison of such records against a Death Master File and to ascertain whether any of the insureds under such policies may be deceased. In December 2013, the CA Controller filed a motion for preliminary injunction seeking the same injunctive relief. A hearing on that motion has been continued until the California Court of Appeals rules on a preliminary injunction order issued in a related case involving an unaffiliated life insurance company, entitled *Chiang v. American National Insurance Company* (the "ANICO Appeal"). The Life Companies have filed a cross-complaint in their case against the CA Controller, seeking a declaration that there is no obligation under California's unclaimed property law to perform a Death Master File comparison and that the Audit Firm cannot obtain the Life Companies' records for the purpose of performing such a comparison. The CA Controller has filed a motion to dismiss the Life Companies' cross-complaint, contending that the Life Companies' request for a declaratory judgment of their rights and obligations under California's unclaimed property law is premature and not ripe for adjudication. A hearing on that motion has also been continued by the court until the Court of Appeals issues its decision in the ANICO Appeal. In July 2014, the court granted a motion by the CA Controller to stay the litigation in its entirety, including all discovery, pending a decision by the Court of Appeals in the ANICO Appeal. Oral argument in the ANICO Appeal has been scheduled for February 2015 with a decision likely by the end of the second quarter of 2015. The current stay of the CA Controller's case against the Life Companies means that no substantive ruling is likely to occur before late 2015. In related activity, the CA Controller's petition for coordination of the lawsuits pending in CA involving its unclaimed property audits of five life insurers, including the lawsuit against the Life Companies, seeking to have them all heard by the same court was denied in January 2015. Pending the outcome of this litigation, the Life Companies have not produced any of their in-force policy records to the CA Controller.

The Life Companies are the subject of a multi-state market conduct examination by five state insurance regulators, which examination is focused on the Life Companies' claim settlement and policy administration practices, and specifically their compliance with state unclaimed property statutes (the "Multi-State Exam"). In July 2013, the Life Companies received requests from the Illinois Department of Insurance, as the managing lead state for the Multi-State Exam, for a significant volume of information beyond that which the Life Companies had already produced, including all of the subject Life Companies' records of in-force policies and other information of the type requested by the Audit Firm as part of the Treasurers' Audit and which is the subject of the CA Controller's complaint. This request prompted the Illinois litigation noted below. In August 2014, the Illinois Department of Insurance appointed a law firm to act as an additional examiner in the Multi-State Exam, which remains ongoing.

In September 2013, certain of the Life Companies filed declaratory judgment actions against the insurance regulators in four states participating in the Multi-State Exam (Illinois, California, Pennsylvania and Florida), asking the courts in those states to declare that applicable insurance laws do not require life insurers to search a Death Master File to ascertain whether insureds are deceased, and to further declare that the regulators in those states do not have legal authority to (i) obtain life insurers' policy records for the purpose of comparing data from those records against a Death Master File, and/or (ii) impose payment obligations on life insurers before a claim and due proof of death have been submitted by policy beneficiaries. In response to the Illinois declaratory judgment action, the Illinois Department of Insurance and its Director (collectively, the "IDOI") filed a motion to dismiss, and in July 2014, the court in Illinois denied, in part, such motion. Specifically, the court allowed to stand the count in the Life Companies' complaint that

the IDOI cannot compel the Life Companies to provide their policy records to the IDOI or persons acting on the IDOI's behalf so as to permit a comparison against the DMF for purposes of identifying deceased insureds, as well as the associated claim for injunctive relief. The court dismissed with prejudice the other counts in the complaint. In August 2014, the IDOI filed its answer to the counts of the complaint that the Illinois court allowed to stand, and in October 2014, the Life Companies filed a motion for summary judgment with respect to those remaining counts. The

IDOI filed cross motions for summary judgment in December 2014. Formal briefing and a hearing schedule on the summary judgment motions are expected to be set by the court at a May 2015 status conference. The Life Companies' actions against regulators in Pennsylvania and Florida are currently stayed by agreement of the parties pending the outcome of the Illinois action. The action against regulators in California, which was filed as part of a counterclaim in the CA Controller litigation, is stayed as described above.

Should these various efforts by state officials succeed in retroactively imposing new claims handling and escheatment requirements with regard to previously issued life insurance policies, such requirements could have a material adverse effect on the Company's profitability, financial position and cash flows. The Company's stance in opposition to the aforementioned actions by state legislators, Treasurers and insurance regulators, including the Life Company's initiation of the litigation described above, also creates a risk of reputational damage to the Company among various constituencies (including its principal insurance regulators, rating agencies, investors, insurance agents and policyholders), particularly if the Company's position is not ultimately vindicated.

See Note 22, "Contingencies," to the Consolidated Financial Statements and the sections of the MD&A entitled "Life & Health Insurance" and "Liquidity and Capital Resources" for additional information on the legal proceedings, including lawsuits, regulatory examinations and inquiries, and other matters described above.

Kemper's insurance subsidiaries are subject to significant regulation, and emerging practices in the evolving legal and regulatory landscape in which they operate could result in increased operating costs, reduced profitability and limited growth.

Kemper's insurance subsidiaries operate under an extensive insurance regulatory system. Current laws and regulations encompass a wide variety of matters, including policy forms, premium rates, licensing, market conduct, trade practices, claims practices, reserve and loss ratio requirements, investment standards, statutory capital and surplus requirements, restrictions on the payment of dividends, approvals of transactions involving a change in control of one or more insurance companies, restrictions on transactions among affiliates and consumer privacy. They also require the filing of annual and quarterly financial reports and reports on holding company issues and other matters.

Pre-approval requirements restrict the companies from implementing premium rate changes for property, casualty and health insurance policies, introducing new, or making changes to existing, policy forms and many other actions.

Insurance regulators conduct periodic examinations of Kemper's insurance subsidiaries and can suspend or delay their operations or licenses, require corrective actions, and impose penalties or other remedies available for compliance failures. For a more detailed discussion of the regulations applicable to Kemper's subsidiaries and these new developments, see "Regulation" in Item 1, beginning on page 10.

These laws and regulations, and their interpretation by the various regulators and courts, are undergoing continual revision and expansion. The legal and regulatory landscape within which Kemper's insurance subsidiaries conduct their businesses is often unpredictable. As industry practices and regulatory, judicial, political, social and other conditions change, unexpected and unintended issues may emerge. These emerging practices, conditions and issues could adversely affect Kemper's insurance subsidiaries in a variety of ways, including, for example, by expansion of coverages beyond their underwriting intent, increasing the number or size of claims or accelerating the payment of claims. Industry practices that were considered approved or legally-compliant and reasonable for years may suddenly be deemed unacceptable by virtue of an unexpected court or regulatory ruling or changes in regulatory enforcement policies and practices. One example is the changing application by various state officials of state unclaimed property laws and related claims handling practices that is discussed in the preceding risk factor. Anticipating such shifts in the law and the impact they may have on the Company and its operations is a difficult task and there can be no assurances that the Company will not encounter such shifts in the future.

The financial market turmoil has resulted in additional scrutiny and proposed regulation of the financial services industry, including insurance companies and their holding company systems. While it is not possible to predict how new laws or regulations or new interpretations of existing laws and regulations may impact the operations of Kemper's insurance subsidiaries, several recent developments have the potential to significantly impact such operations. This includes state adoption of extensive modifications to the IHCS that will, among other things, substantially expand the oversight and examination powers of state insurance regulators beyond licensed insurance companies to their non-insurance affiliates and impose new reporting requirements with respect to, among other things, enterprise risk to the organization as a whole, affiliated transactions, and any divestiture of controlling interests in an insurer. In

addition, federal legislation has resulted in regulations affecting health insurers under the Health Care Acts, and potential changes to the state insurance regulatory system may result from the DFA. See the discussion of the NAIC model act and the DFA under “Regulation” in Item 1, beginning on page 10.

These new developments and significant changes in, or new interpretations of, existing laws and regulations could make it more expensive for Kemper’s insurance subsidiaries to conduct and grow their businesses.

Legal and regulatory proceedings are unpredictable and, in particular, the phenomenon of runaway jury verdicts could result in one or more unexpected verdicts against the Company that could have a material adverse effect on the Company's financial results for any given period.

Kemper and its subsidiaries are from time to time involved in lawsuits, regulatory inquiries, and other legal proceedings arising out of the ordinary course of their businesses. Some of these proceedings may involve matters particular to Kemper or one or more of its subsidiaries, while others may pertain to business practices in the industry in which Kemper and its subsidiaries operate. Some lawsuits may seek class action status that, if granted, could expose the Company to potentially significant liability by virtue of the size of the putative classes. These matters raise difficult factual and legal issues and are subject to uncertainties and complexities. The outcomes of these matters are difficult to predict, and the amounts or ranges of potential loss at particular stages in the proceedings are in most cases difficult or impossible to ascertain. A further complication is that even where the possibility of an adverse outcome is deemed to be remote using traditional legal analysis, juries sometimes can and do substitute their subjective views in place of facts and established legal principles. Given the unpredictability of the legal and regulatory landscape in which the Company operates, there can be no assurance that one or more of these matters will not produce a result that could have a material adverse effect on the Company's financial results for any given period.

For information about the Company's pending litigation, see Note 22, "Contingencies," to the Consolidated Financial Statements.

Catastrophe losses could materially and adversely affect the Company's results of operations, liquidity and/or financial condition, the availability of reinsurance and the ratings of Kemper and its insurance subsidiaries.

Kemper's property and casualty insurance subsidiaries are subject to claims arising out of catastrophes that may have a significant effect on their results of operations, liquidity and financial condition. Catastrophes can be caused by various events, including, but not limited to, hurricanes, tornadoes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and wildfires and may include man-made events, such as terrorist attacks and hazardous material spills. The incidence, frequency and severity of catastrophes are inherently unpredictable and may be impacted by the uncertain effects of climate change. The extent of the Company's losses from a catastrophe is a function of both the total amount of insured exposure in the geographic area affected by the event and the severity of the event. The Company could experience more than one severe catastrophic event in any given period.

Kemper's life and health insurance subsidiaries are particularly exposed to risks of catastrophic mortality, such as pandemic or other events that result in large numbers of deaths. In addition, the occurrence of such an event in a concentrated geographic area could have a severe disruptive effect on the Company's workforce and business operations. The likelihood and severity of such events cannot be predicted and are difficult to estimate.

The Company uses catastrophe modeling tools developed by third parties to project its potential exposure to catastrophic events under various scenarios. Such models are based on various assumptions and judgments which may turn out to be wrong. The actual impact of one or more catastrophic events could adversely and materially differ from these projections.

Kemper's insurance subsidiaries seek to reduce their exposure to catastrophe losses through the purchase of catastrophe reinsurance. Reinsurance does not relieve Kemper's insurance subsidiaries of their direct liability to their policyholders. As long as the reinsurers meet their obligations, the net liability for Kemper's insurance subsidiaries is limited to the amount of risk that they retain. While the Company's principal reinsurers are each rated "A-" or better by A.M. Best at the time reinsurance is purchased, the Company cannot be certain that reinsurers will pay the amounts due from them either now, in the future, or on a timely basis. A reinsurer's insolvency or inability to make payments under the terms of its reinsurance agreement could have a material adverse effect on the Company's financial position, results of operations and liquidity.

In addition, market conditions beyond the Company's control determine the availability of the reinsurance protection that Kemper's insurance subsidiaries may purchase. A decrease in the amount of reinsurance protection that Kemper's insurance subsidiaries purchase generally should increase their risk of a more severe loss. However, if the amount of available reinsurance is reduced, Kemper's insurance subsidiaries may be forced to incur additional expenses for reinsurance or may not be able to obtain sufficient reinsurance on acceptable terms, which could adversely affect the ability of Kemper's insurance subsidiaries to write future insurance policies or result in their retaining more risk with respect to such policies.

Kemper's insurance subsidiaries also manage their exposure to catastrophe losses through underwriting strategies such as reducing exposures in, or withdrawing from, catastrophe-prone areas, establishing appropriate guidelines for insurable structures, and setting appropriate rates, deductibles, exclusions and policy limits. The extent to which Kemper's insurance subsidiaries can manage their exposure through such strategies may be limited by law or regulatory action. For example, laws

and regulations may limit the rate or timing at which insurers may non-renew insurance policies in catastrophe-prone areas or require insurers to participate in wind pools and joint underwriting associations. Generally, an insurer's participation in such pools and associations are based on the insurer's market share determined on a state-wide basis. Accordingly, even though Kemper's insurance subsidiaries may not incur a direct insured loss as a result of managing direct catastrophe exposures, they may incur indirect losses from required participation in pools and associations. Laws and regulations requiring prior approval of policy forms and premium rates may limit the ability of Kemper's insurance subsidiaries to increase rates or deductibles on a timely basis, which may result in additional losses or lower returns than otherwise would have occurred in an unregulated market. See the risk factor above under the title "Kemper's insurance subsidiaries are subject to significant regulation, and emerging practices in the evolving legal and regulatory landscape in which they operate could result in increased operating costs, reduced profitability and limited growth."

If the catastrophic risk retained by Kemper's insurance subsidiaries increases, rating agencies may downgrade the ratings of Kemper and/or its insurance subsidiaries or require Kemper to retain more capital in its insurance businesses to maintain existing ratings. See the risk factor below under the title "A significant downgrade in the ratings of Kemper or its insurance subsidiaries could adversely affect the Company."

A significant downgrade in the ratings of Kemper or its insurance subsidiaries could adversely and materially affect the Company.

Third-party rating agencies assess the financial strength and rate the claims-paying ability of insurance companies based on criteria established by the rating agencies. Third-party ratings are important competitive factors in the insurance industry. Financial strength ratings are used to assess the financial strength and quality of insurers. A significant downgrade by A.M. Best in the ratings of Kemper's insurance subsidiaries, particularly those operating in the preferred and standard market or offering homeowners insurance, could result in a substantial loss of business if agents or policyholders of such subsidiaries move to other companies with higher claims-paying and financial strength ratings. Any substantial loss of business could have a material adverse effect on the financial condition and results of operations of such subsidiaries. A downgrade in Kemper's credit rating by Standard & Poor's ("S&P"), Moody's Investors Services ("Moody's") or Fitch Ratings ("Fitch") may reduce Kemper's ability to access the capital markets for general corporate purposes or refinance existing debt.

The insurance industry is highly competitive.

The Company's insurance businesses face significant competition, and their ability to compete is affected by a variety of issues relative to others in the industry, such as product pricing, service quality, financial strength and name recognition. Competitive success is based on many factors, including, but not limited to, the following:

- Competitiveness of prices charged for insurance policies;
- Sophistication of pricing segmentation;
- Selection of agents and other business partners;
- Compensation paid to agents;
- Underwriting discipline;
- Selectiveness of sales markets;
- Effectiveness of marketing materials and name recognition;
- Product and technological innovation;
- Ability to detect and prevent fraudulent insurance claims;
- Ability to control operating expenses;
- Financial strength ratings; and
- Quality of services provided to, and ease of doing business with, agents and policyholders.

The inability to compete effectively in any of the Company's insurance businesses could materially reduce the Company's customer base and revenues and could adversely affect the future results and financial condition of the Company.

See "Competition" in Item 1 of Part I beginning on page 7 and page 10, for more information on the competitive rankings in the property and casualty insurance markets and the life and health insurance markets, respectively, in the United States.

Reserve National's operating history with its expanded distribution channels and new products is limited.



Reserve National's business model, which has traditionally focused on providing limited benefit and supplemental accident and health insurance coverages to persons who lack access to traditional private options, was adversely affected by the Health Care Acts. In response, Reserve National has adapted its business model by placing emphasis on designing and selling supplemental health insurance products that are not expected to be as severely impacted by the Health Care Acts and ceasing to issue health

insurance products that are more severely impacted. Because Reserve National's operating history with respect to some of these supplemental health insurance products is limited, it supplements its data with industry data and experience in determining rates to charge for these products and projecting returns. It will take several years to develop company-specific experience. Reserve National's actual experience could adversely and materially differ from the data and experience on which assumptions and projections are based.

Reserve National has expanded its distribution channels over the past two years, launching Kemper Senior Solutions and Kemper Benefits. Kemper Senior Solutions markets small face value, or final expense, life insurance and home health care products focusing on the individual senior age demographic of the market place. Kemper Benefits sells voluntary supplemental insurance products in the employer marketplace. Brokers and non-exclusive independent agents are utilized to market and distribute products in these new distribution channels. Reserve National appointed approximately 20,000 independent agents during the past two years in connection with these initiatives. Reserve National has limited history on how some of its products will perform using these distribution channels. It will take several years to determine if actual performance meets, exceeds or is below expectations. If performance is below expectations, Reserve National's financial position, returns and valuation could be adversely and materially impacted for many years due to the long-term nature of some of the products sold through these distribution channels. Failure to maintain the security of personal data and the availability of critical systems may result in lost business, reputational harm, and legal costs and regulatory penalties.

Kemper's insurance subsidiaries obtain and store vast amounts of personal data that can present significant risks to the Company and its customers and employees. An increasing array of laws and regulations govern the use and storage of such data, including, for example, social security numbers, credit card data and personal health information. The Company's data systems are vulnerable to security breaches due to the sophistication of cyber-attacks, viruses, malware, hackers and other external hazards, as well as inadvertent errors, equipment and system failures, and employee misconduct. The Company also relies on the ability of its business partners to maintain secure systems and processes that comply with legal requirements and protect personal data. These increased risks and expanding regulatory requirements related to personal data security expose the Company to potential data loss and resulting damages, reputational risk and significant increases in compliance and litigation costs. In the event of non-compliance with the Payment Card Industry Data Security Standard, an information security standard for organizations that handle cardholder information for the major debit, credit, prepaid, e-purse, ATM and point-of-sale cards, such organizations could prevent Kemper's insurance subsidiaries from collecting premium payments from customers by way of such cards and impose significant fines on Kemper's insurance subsidiaries.

The Company's business operations rely on the continuous availability of its computer systems. In addition to disruptions caused by cyber-attacks or other data breaches, such systems may be adversely affected by natural and man-made catastrophes. The Company's failure to maintain business continuity in the wake of such events may prevent the timely completion of critical processes across its operations, including, for example, insurance policy administration, claims processing, billing, treasury and investment operations and payroll. These failures could result in significant loss of business, fines and litigation.

The Company's investment portfolio is exposed to a variety of risks that may negatively impact net investment income and cause realized and unrealized losses.

The Company maintains a diversified investment portfolio that is exposed to significant financial and capital market risks, including interest rate (risk-free and spread), equity price, and liquidity, as well as risks from changes in tax laws and regulations and other risks from changes in general economic conditions.

The interest rate environment has a significant impact on the Company's financial results and position. In recent years, rates have been at or near historic lows. A protracted low interest rate environment would continue to place pressure on net investment income, particularly related to fixed income securities, short-term investments and limited liability investment companies and limited partnerships accounted for under the equity method of accounting ("Equity Method Limited Liability Investments") that invest in distressed and mezzanine debt of other companies. A decline in interest rates would generally increase the carrying value of the Company's fixed income securities and its Equity Method Limited Liability Investments that exhibit debt-like characteristics, but it may have an adverse effect on the Company's investment income as it invests cash in new investments that may yield less than the portfolio's average rate. In a

declining interest rate environment, borrowers may seek to refinance their borrowings at lower rates and, accordingly, prepay or redeem securities the Company holds as investments more quickly than the Company initially expected. Such prepayment or redemption action may cause the Company to reinvest the redeemed proceeds in lower yielding investments. An increase in interest rates would generally reduce the carrying value of a substantial portion of the Company's investment portfolio, particularly fixed income securities and Equity Method Limited Liability Investments, which typically provide higher returns but at a higher risk.

The Company invests a portion of its investment portfolio in equity securities, which generally have more volatile returns than fixed income securities and may experience sustained periods of depressed values. There are multiple factors that could negatively impact the performance of the Company's equity portfolio, including general economic conditions, industry or sector deterioration and issuer-specific concerns. A decline in equity values may result in a decrease in dividend income, realized losses upon sales of the securities, or other-than-temporary impairment charges on securities still held.

Interest rates and equity returns also have a significant impact on the Company's pension and postretirement employee benefit plans. In addition to the impact on carrying values and yields of the underlying assets of the funded plans, interest rates also impact the discounting of the projected and accumulated benefit obligations of the plans. A decrease in interest rates may have a negative impact on the funded status of the plans.

The nature and cash flow needs of the Company and the insurance industry in general present certain liquidity risks that may impact the return of the investment portfolio. If the Company were to experience several significant catastrophic events over a relatively short period of time, investments may have to be sold in advance of their maturity dates to fund payments to claimants, which could result in realized losses. Additionally, increases in illiquidity in the financial markets may increase uncertainty in the valuations of the Company's investments. This increases the risk that the fair values reported in the Company's consolidated financial statements may differ from the actual price that may be obtained in an orderly sales transaction.

The Company has also benefited from certain tax laws related to its investment portfolio, including dividends received deductions and tax-exempt municipal securities. Changes in tax laws may have a detrimental effect on the after-tax return of the Company's investment portfolio.

The Company's entire investment portfolio is subject to broad risks inherent in the financial markets, including, but not limited to, inflation, regulatory changes, inactive capital markets, governmental and social stability, economic outlooks, unemployment and recession. Changes to these risks and how the market perceives them may impact the financial performance of the Company's investments.

Kemper and its insurance subsidiaries are subject to various risk rating and capital adequacy measurements that are significantly impacted by various characteristics of their invested assets, including, but not limited to, asset type, class and credit rating. The Company's insurance subsidiaries are also subject to various limitations on the amounts at which they can invest in individual assets or certain asset classes in the aggregate. Asset risk is one factor used by insurance regulators and rating agencies to determine required capital for Kemper's insurance subsidiaries. Accordingly, a deterioration in the quality of the investments held by Kemper's insurance subsidiaries or an increase in the investment risk inherent in their investment portfolios could increase capital requirements. See risk factor below under the title "Kemper relies on receiving dividends from its subsidiaries to service its debt, to pay dividends to its shareholders and/or make repurchases of its stock." These factors may inhibit the Company from shifting its investment mix to produce higher returns. The Company is also subject to concentration of investment risk to the extent that the portfolio is heavily invested, at any particular time, in specific asset types, classes, industries, sectors or collateral types, among other defining features. Developments and the market's perception thereof in any of these concentrations may exacerbate the negative effects on the Company's investment portfolio compared to other companies.

Estimating losses and LAE for determining property and casualty insurance reserves, or determining premium rates, is inherently uncertain, and the Company's results of operations may be materially impacted if the Company's insurance reserves or premium rates are insufficient.

The Company establishes loss and LAE reserves to cover estimated liabilities, which remain unpaid as of the end of each accounting period, and to investigate and settle all claims incurred under the property and casualty insurance policies that it has issued. Loss and LAE reserves are established for claims that have been reported to the Company as of the end of the accounting period, as well as for claims that have occurred but have not yet been reported to the Company. The estimates of loss and LAE reserves are based on the Company's assessment of the facts and circumstances known to it at the time, as well as estimates of the impact of future trends in the severity of claims, the frequency of claims and other factors. See MD&A, "Critical Accounting Estimates," under the caption "Property and Casualty Insurance Reserves for Losses and Loss Adjustment Expenses" beginning on page 53 for a discussion of the Company's reserving process and the factors considered by the Company's actuaries in estimating the Company's Property and Casualty Insurance Reserves.

The process of estimating property and casualty insurance reserves is complex and imprecise. The reserves established by the Company are inherently uncertain estimates and could prove to be inadequate to cover its ultimate losses and expenses for insured events that have occurred. The estimate of the ultimate cost of claims for insured events that have occurred must take

into consideration many factors that are dependent on the outcome of future events associated with the reporting, investigation and settlement of claims. The impacts on the Company's estimates of property and casualty insurance reserves from these factors are difficult to assess accurately. A change in any one or more of the factors is likely to result in a projected ultimate loss that is different than the previous projected ultimate loss and may have a material impact on the Company's estimate of the projected ultimate loss. Increases in the estimates of ultimate losses and LAE will decrease earnings, while decreases in such estimates will increase earnings, as reported by the Company in the results of its operations for the periods in which the changes to the estimates are made by the Company.

The Company's actuaries also consider trends in the severity and frequency of claims and other factors when determining the premium rates to charge for its property and casualty insurance products. An unanticipated change in any one or more of these factors or trends, as well as a change in competitive conditions, may also result in inadequate premium rates charged for insurance policies issued by Kemper's property and casualty insurance subsidiaries in the future. Such pricing inadequacies could have a material impact on the Company's operating results.

Kemper relies on receiving dividends from its subsidiaries to service its debt, to pay dividends to its shareholders and/or make repurchases of its stock.

As a holding company with no business operations of its own, Kemper depends on the dividend income that it receives from its subsidiaries as the primary source of funds to pay interest and principal on its outstanding debt obligations, to pay dividends to its shareholders and to make repurchases of its stock. Kemper's insurance subsidiaries are subject to significant regulatory restrictions under state insurance laws and regulations that limit their ability to declare and pay dividends. These laws and regulations impose minimum solvency and liquidity requirements on dividends between affiliated companies and require prior notice to, and may require approval from, state insurance regulators before dividends can be paid. In addition, third-party rating agencies monitor statutory capital and surplus levels for capital adequacy. Even though a dividend may be payable without regulatory approval, an insurance subsidiary may forgo paying a dividend to Kemper and retain the capital in its insurance subsidiaries to maintain or improve the ratings of Kemper's insurance subsidiaries. The inability of one or more of Kemper's insurance subsidiaries to pay sufficient dividends to Kemper may materially affect Kemper's ability to pay its debt obligations on time, to pay dividends to its shareholders or make repurchases of its stock.

Managing technology initiatives to address business developments and regulatory requirements present significant challenges to the Company.

While technological developments can streamline many business processes and ultimately reduce the cost of operations, technology initiatives can present short-term cost and implementation risks. In addition, projections of expenses and implementation schedules may be inaccurate and can escalate over time, while the ultimate utility of a technology initiative could deteriorate over time. The financial services industry is highly regulated, and the Company faces rising costs and competing time constraints in adapting technology to meet compliance requirements of new and proposed regulations.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

Owned Properties

Kemper's subsidiaries together own and occupy 13 buildings located in seven states consisting of approximately 49,000 square feet in the aggregate. Kemper's subsidiaries hold additional properties that are not occupied by Kemper or its subsidiaries solely for investment purposes.

#### Leased Facilities

The Company leases five floors, or approximately 67,000 square feet, in a 41-story office building in Chicago for its corporate headquarters and Property & Casualty Insurance segment's headquarters. The lease expires in September 2023. Kemper's Property & Casualty Insurance segment leases facilities with an aggregate square footage of approximately 413,000 at 10 locations in eight states. The latest expiration date of the existing leases is in September 2023. Kemper's Life & Health Insurance segment leases facilities with aggregate square footage of approximately 460,000 at 127 locations in 27 states. The latest expiration date of the existing leases is in January 2025. Kemper's corporate data processing operation leases facilities with aggregate square footage of approximately 36,000 square feet at two locations in two states. The latest expiration date of the existing leases is in December 2018.

The properties described above are in good condition. The properties utilized in the Company's operations consist of facilities suitable for general office space, call centers and data processing operations.

#### Item 3. Legal Proceedings.

##### Proceedings

Information concerning pending legal proceedings is incorporated herein by reference to Note 22, "Contingencies," to the Consolidated Financial Statements.

#### Item 4. Mine Safety Disclosures.

Not applicable.

## PART II

## Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

## Market Information

Kemper's common stock is traded on the New York Stock Exchange (the "NYSE") under the symbol of "KMPR."

Quarterly information pertaining to market prices of Kemper common stock in 2014 and 2013 is presented below.

DOLLARS PER SHARE	Three Months Ended				Year Ended
	Mar 31, 2014	Jun 30, 2014	Sep 30, 2014	Dec 31, 2014	Dec 31, 2014
Common Stock Market Prices:					
High	\$40.99	\$40.51	\$37.57	\$37.63	\$40.99
Low	35.63	33.64	31.82	32.66	31.82
Close	39.17	36.86	34.15	36.11	36.11

DOLLARS PER SHARE	Three Months Ended				Year Ended
	Mar 31, 2013	Jun 30, 2013	Sep 30, 2013	Dec 31, 2013	Dec 31, 2013
Common Stock Market Prices:					
High	\$33.88	\$34.79	\$36.56	\$41.31	\$41.31
Low	29.87	30.43	33.23	33.49	29.87
Close	32.61	34.25	33.60	40.88	40.88

## Holders

As of January 20, 2015, the number of record holders of Kemper's common stock was 4,192.



## Dividends

Quarterly information pertaining to payment of dividends on Kemper's common stock is presented below.

DOLLARS PER SHARE	Three Months Ended				Year Ended
	Mar 31, 2014	Jun 30, 2014	Sep 30, 2014	Dec 31, 2014	Dec 31, 2014
Cash Dividends Paid to Shareholders (per share)	\$0.24	\$0.24	\$0.24	\$0.24	\$0.96

DOLLARS PER SHARE	Three Months Ended				Year Ended
	Mar 31, 2013	Jun 30, 2013	Sep 30, 2013	Dec 31, 2013	Dec 31, 2013
Cash Dividends Paid to Shareholders (per share)	\$0.24	\$0.24	\$0.24	\$0.24	\$0.96

Kemper's insurance subsidiaries are subject to various state insurance laws that may restrict the ability of these insurance subsidiaries to pay dividends without prior regulatory approval. See MD&A, "Liquidity and Capital Resources" and Note 8, "Shareholders' Equity," to the Consolidated Financial Statements for information on Kemper's ability and intent to pay dividends.

## Issuer Purchases of Equity Securities

Information pertaining to purchases of Kemper common stock for the three months ended December 31, 2014 follows.

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (Dollars in Millions)
October 1 - October 31	—	N/A	—	\$300.0
November 1 - November 30	—	N/A	—	\$300.0
December 1 - December 31	258,306	\$34.94	258,306	\$291.0

(1) On August 6, 2014, Kemper's Board of Directors authorized the repurchase of up to \$300 million worth of Kemper's common stock. The repurchase program has no expiration date. See MD&A, "Liquidity and Capital Resources."

Kemper Common Stock Performance Graph

The following graph assumes \$100 invested on December 31, 2009 in (i) Kemper common stock, (ii) the S&P MidCap 400 Index and (iii) the S&P Supercomposite Insurance Index, in each case with dividends reinvested. Kemper is a constituent of each of these two indices.

The comparisons in the graph below are based on historical data and are not intended to forecast the possible future performance of Kemper common stock.

Company / Index	2009	2010	2011	2012	2013	2014
Kemper Corporation	\$100.00	\$115.34	\$142.06	\$148.20	\$211.19	\$191.54
S&P MidCap 400 Index	100.00	126.64	124.45	146.69	195.84	214.97
S&P Supercomposite Insurance Index	100.00	116.03	108.01	128.66	187.52	203.86

## Item 6. Selected Financial Data.

Selected financial information as of and for the years ended December 31, 2014, 2013, 2012, 2011 and 2010 is presented below.

DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS FOR THE YEAR	2014	2013	2012	2011	2010
Earned Premiums	\$1,862.2	\$2,025.8	\$2,107.1	\$2,173.6	\$2,289.4
Net Investment Income	309.1	314.7	295.9	298.0	325.7
Other Income	1.4	0.8	0.8	1.0	1.3
Net Realized Gains on Sales of Investments	39.1	99.1	65.4	33.7	42.6
Net Impairment Losses Recognized in Earnings	(15.2 )	(13.9 )	(6.9 )	(11.3 )	(16.5 )
Total Revenues	\$2,196.6	\$2,426.5	\$2,462.3	\$2,495.0	\$2,642.5
Income from Continuing Operations	\$112.6	\$214.5	\$91.8	\$61.7	\$162.4
Income from Discontinued Operations	1.9	3.2	11.6	12.8	15.5
Net Income	\$114.5	\$217.7	\$103.4	\$74.5	\$177.9
Per Unrestricted Share:					
Income from Continuing Operations	\$2.08	\$3.75	\$1.55	\$1.02	\$2.62
Income from Discontinued Operations	0.04	0.06	0.20	0.21	0.25
Net Income	\$2.12	\$3.81	\$1.75	\$1.23	\$2.87
Per Unrestricted Share Assuming Dilution:					
Income from Continuing Operations	\$2.08	\$3.74	\$1.54	\$1.02	\$2.62
Income from Discontinued Operations	0.04	0.06	0.20	0.21	0.25
Net Income	\$2.12	\$3.80	\$1.74	\$1.23	\$2.87
Dividends Paid to Shareholders Per Share	\$0.96	\$0.96	\$0.96	\$0.96	\$0.88
AT YEAR END					
Total Assets	\$7,833.4	\$7,656.4	\$8,009.1	\$7,934.7	\$8,260.8
Insurance Reserves	\$4,007.6	\$4,061.0	\$4,132.2	\$4,131.8	\$4,182.4
Unearned Premiums	536.9	598.9	650.9	666.2	678.6
Certificates of Deposits	—	—	—	—	321.4
Debt	752.1	606.9	611.4	610.6	609.8
All Other Liabilities	446.1	338.1	452.9	409.5	445.6
Total Liabilities	5,742.7	5,604.9	5,847.4	5,818.1	6,237.8
Shareholders' Equity	2,090.7	2,051.5	2,161.7	2,116.6	2,023.0
Total Liabilities and Shareholders' Equity	\$7,833.4	\$7,656.4	\$8,009.1	\$7,934.7	\$8,260.8
Book Value Per Share	\$39.88	\$36.86	\$36.98	\$35.13	\$33.13

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

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Management's Discussion and Analysis of  
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Kemper Corporation and Subsidiaries  
Management's Discussion and Analysis of Financial Condition and Results of Operations

## SUMMARY OF RESULTS

Net Income was \$114.5 million (\$2.12 per unrestricted common share) for the year ended December 31, 2014, compared to \$217.7 million (\$3.81 per unrestricted common share) for the year ended December 31, 2013. Income from Continuing Operations was \$112.6 million (\$2.08 per unrestricted common share) in 2014, compared to \$214.5 million (\$3.75 per unrestricted common share) in 2013.

A reconciliation of Total Segment Net Operating Income to Net Income for the years ended December 31, 2014, 2013 and 2012 is presented below:

DOLLARS IN MILLIONS	2014	2013	Increase (Decrease) from 2013 to 2014	2012	Increase (Decrease) from 2012 to 2013
Segment Net Operating Income (Loss):					
Property & Casualty Insurance	\$24.9	\$100.6	\$(75.7)	\$(10.9)	\$111.5
Life & Health Insurance	91.8	89.3	2.5	90.8	(1.5)
Total Segment Net Operating Income	116.7	189.9	(73.2)	79.9	110.0
Unallocated Net Operating Loss	(19.6)	(30.7)	11.1	(26.1)	(4.6)
Consolidated Net Operating Income	97.1	159.2	(62.1)	53.8	105.4
Net Income (Loss) From:					
Net Realized Gains on Sales of Investments	25.4	64.4	(39.0)	42.5	21.9
Net Impairment Losses Recognized in Earnings	(9.9)	(9.1)	(0.8)	(4.5)	(4.6)
Income from Continuing Operations	112.6	214.5	(101.9)	91.8	122.7
Income from Discontinued Operations	1.9	3.2	(1.3)	11.6	(8.4)
Net Income	\$114.5	\$217.7	\$(103.2)	\$103.4	\$114.3

The Company's results and the results in the Property & Casualty Insurance segment were significantly and negatively impacted in 2014, compared to 2013, by the level of catastrophe losses and LAE and a charge to write off certain internal use software. Catastrophe losses and LAE in the Property & Casualty Insurance segment (excluding loss and LAE reserve development from prior accident years) were \$96.5 million before taxes for the year ended December 31, 2014, compared to \$47.1 million in 2013, an increase of \$49.4 million. See MD&A, "Catastrophes," beginning on page 28 for a discussion of the impact of catastrophe losses and LAE on the Company's results and MD&A, "Property & Casualty Insurance," beginning on page 31 for a discussion of the impact of catastrophe losses and LAE on the Property & Casualty Insurance segment's results. Results for the Property & Casualty Insurance segment in 2014 also include a charge of \$54.6 million before taxes to write off certain internal use software. See MD&A, "Write-off of Long-lived Asset," beginning on page 48 for more information related to the internal use software write-off.

## Revenues

Earned Premiums were \$1,862.2 million in 2014, compared to \$2,025.8 million in 2013, a decrease of \$163.6 million. Earned Premiums decreased by \$143.4 million and \$20.2 million in the Property & Casualty Insurance and Life & Health Insurance segments, respectively.

Net Investment Income decreased by \$5.6 million in 2014 due primarily to \$17.4 million in lower net investment income from Equity Method Limited Liability Investments and \$8.1 million of lower net investment income from Interest and Dividends on Fixed Maturities, partially offset by \$21.9 million of higher net investment income from Dividends on Equity Securities.

Net Realized Gains on Sales of Investments were \$39.1 million in 2014, compared to \$99.1 million in 2013. The Company sold the building where Kemper's corporate offices are headquartered and recognized a realized gain of \$43.6 million in 2013.

Net Impairment Losses Recognized in Earnings for the years ended December 31, 2014 and 2013 were \$15.2 million and \$13.9 million, respectively.

The Company cannot predict when or if similar investment gains or losses may occur in the future. See MD&A, "Investment Results," for additional information pertaining to investment performance.

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## CATASTROPHES

Catastrophes and natural disasters are inherent risks of the property and casualty insurance business. These catastrophic events and natural disasters include, without limitation, hurricanes, tornadoes, earthquakes, hailstorms, wildfires, high winds and winter storms. Such events result in insured losses that are, and will continue to be, a material factor in the results of operations and financial position of the Company's property and casualty insurance companies. Further, because the level of these insured losses occurring in any one year cannot be accurately predicted, these losses may contribute to material year-to-year fluctuations in the results of operations and financial position of these companies. Specific types of catastrophic events are more likely to occur at certain times within the year than others. This factor adds an element of seasonality to property and casualty insurance claims. The Company has adopted the industry-wide catastrophe classifications of storms and other events promulgated by ISO to track and report losses related to catastrophes. ISO classifies a disaster as a catastrophe when the event causes \$25.0 million or more in direct insured losses to property and affects a significant number of policyholders and insurers. ISO-classified catastrophes are assigned a unique serial number recognized throughout the insurance industry. The discussions that follow utilize ISO's definition of catastrophes.

The number of catastrophic events and catastrophe losses and LAE (excluding loss and LAE reserve development) by range of loss and business segment for the years ended December 31, 2014, 2013 and 2012 are presented below:

DOLLARS IN MILLIONS	Year Ended		Year Ended		Year Ended	
	Dec 31, 2014	Dec 31, 2014	Dec 31, 2013	Dec 31, 2013	Dec 31, 2012	Dec 31, 2012
	Number of Events	Losses and LAE	Number of Events	Losses and LAE	Number of Events	Losses and LAE
Range of Losses and LAE Per Event:						
Below \$5	27	\$31.1	27	\$44.3	19	\$25.6
\$5 - \$10	3	20.4	1	6.4	5	39.4
\$10 - \$15	1	13.1	—	—	1	11.0
\$15 - \$20	—	—	—	—	—	—
\$20 - \$25	—	—	—	—	—	—
Greater Than \$25	1	33.9	—	—	1	48.5
Total	32	\$98.5	28	\$50.7	26	\$124.5
Property & Casualty Insurance		\$96.5		\$47.1		\$118.5
Life & Health Insurance		2.0		3.6		6.0
Total Catastrophe Losses and LAE		\$98.5		\$50.7		\$124.5

As shown in the preceding table, catastrophe losses and LAE increased for the year ended December 31, 2014, compared to 2013, due primarily to one catastrophe event that exceeded \$25 million of losses and LAE and four other catastrophe events that each exceeded \$5 million of losses and LAE in 2014, compared to only one such event exceeding \$5 million in 2013, partially offset by lower severity of losses below \$5 million per event in 2014, compared to 2013. The Company's results were negatively impacted by the severity of certain events, most notably, two hailstorms occurring in the second quarter. The event in the preceding table with \$33.9 million in catastrophe losses and LAE in 2014 was incurred in multiple states, particularly Montana. The event in the preceding table with \$13.1 million in catastrophe losses and LAE in 2014 was primarily related to hail in Texas.

As shown in the preceding table, catastrophe losses and LAE decreased for the year ended December 31, 2013, compared to 2012, due primarily to only one catastrophe event in the \$5 million to \$10 million range in 2013, compared to one catastrophe event that exceeded \$25 million of losses and LAE and six other catastrophe events that each exceeded \$5 million of losses and LAE in 2012. This was partially offset by higher frequency and severity of losses below \$5 million per event in 2013, compared to 2012. In the fourth quarter of 2012, the Company incurred \$48.5 million in catastrophe losses and LAE in several northeastern states related to Superstorm Sandy. The five events in the \$5 million to \$10 million range and one event in the \$10 million to \$15 million range in 2012 were

related to hail or wind events in either Texas, Colorado or the Midwest and mid-Atlantic states.



## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## CATASTROPHES (Continued)

## Catastrophe Reinsurance

The Company primarily manages its exposure to catastrophes and other natural disasters through a combination of geographical diversification, management of the amount and location of risks insured in certain regions and a primary catastrophe reinsurance program for the Property & Casualty Insurance segment. Coverage for this segment's primary catastrophe reinsurance program is provided in various layers (see Note 19, "Catastrophe Reinsurance," to the Consolidated Financial Statements for further discussion of this program). In addition to this program, the Property & Casualty Insurance segment had a reinsurance treaty covering the three-year period that ended June 1, 2013 for catastrophe losses in North Carolina at retentions lower than its primary catastrophe reinsurance program ("the NC Program"). The Property & Casualty Insurance segment also purchases reinsurance from the FHCF for hurricane losses in Florida at retentions lower than its primary catastrophe reinsurance program. The Life & Health Insurance also purchases reinsurance from the FHCF for hurricane losses in Florida. Except for the coverage provided by the FHCF, the Life & Health Insurance segment did not carry catastrophe reinsurance in 2014 and 2013, primarily due to actions taken by KHSC to reduce its exposures to catastrophes. See Note 19, "Catastrophe Reinsurance," to the Consolidated Financial Statements for information related to the Life & Health Insurance segment's primary catastrophe reinsurance program in 2012.

See the "Reinsurance" subsections of the "Property and Casualty Insurance Business" and "Life and Health Insurance Business" sections of Item 1(c), "Description of Business," and Note 19, "Catastrophe Reinsurance," to the Consolidated Financial Statements for additional information on the Company's reinsurance programs.

## LOSS AND LAE RESERVE DEVELOPMENT

Increases (decreases) in the Company's property and casualty loss and LAE reserves for the years ended December 31, 2014, 2013 and 2012 to recognize adverse (favorable) loss and LAE reserve development from prior accident years in continuing operations, hereinafter also referred to as "reserve development" in the discussion of segment results, is presented below.

DOLLARS IN MILLIONS	2014	2013	2012
Property & Casualty Insurance:			
Non-catastrophe	\$(38.6 )	\$(45.5 )	\$(18.5 )
Catastrophe	(15.8 )	(12.5 )	(6.4 )
Total	(54.4 )	(58.0 )	(24.9 )
Life & Health Insurance:			
Non-catastrophe	(0.2 )	0.2	(0.4 )
Catastrophe	1.1	(2.0 )	0.1
Total	0.9	(1.8 )	(0.3 )
Decrease in Total Loss and LAE Reserves Related to Prior Years:			
Non-catastrophe	(38.8 )	(45.3 )	(18.9 )
Catastrophe	(14.7 )	(14.5 )	(6.3 )
Decrease in Total Loss and LAE Reserves Related to Prior Years	\$(53.5 )	\$(59.8 )	\$(25.2 )

See MD&A, "Property & Casualty Insurance," MD&A, "Life & Health Insurance," and Note 5, "Property and Casualty Insurance Reserves," to the Consolidated Financial Statements for additional information on the Company's reserve development. See MD&A, "Critical Accounting Estimates," of this 2014 Annual Report for additional information pertaining to the Company's process of estimating property and casualty insurance reserves for losses and LAE, and the estimated variability thereof, development of property and casualty insurance losses and LAE, and a discussion of some of the variables that may impact them.

## NON-GAAP FINANCIAL MEASURES

Pursuant to the rules and regulations of the SEC, the Company is required to file consolidated financial statements prepared in accordance with the accounting principles generally accepted in the United States ("GAAP"). The Company is permitted to include non-GAAP financial measures in its filings provided that they are defined along with an

explanation of their usefulness to investors, are no more prominent than the comparable GAAP financial measures and are reconciled to such GAAP financial measures.

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## NON-GAAP FINANCIAL MEASURES (Continued)

These non-GAAP financial measures should not be considered a substitute for the comparable GAAP financial measures, as they do not fully recognize the overall profitability of the Company's business.

## Underlying Combined Ratio

The following discussion for the Property & Casualty Insurance segment uses the non-GAAP financial measures of (i) Underlying Losses and LAE and (ii) Underlying Combined Ratio. Underlying Losses and LAE (also referred to in the discussion as "Current Year Non-catastrophe Losses and LAE") exclude the impact of catastrophe losses, and loss and LAE reserve development from prior years from the Company's Incurred Losses and LAE, which is the most directly comparable GAAP financial measure. The Underlying Combined Ratio is computed by adding the Current Year Non-catastrophe Losses and LAE Ratio with the Insurance Expense (including write-offs of long-lived assets) Ratio. The most directly comparable GAAP financial measure is the Combined Ratio, which is computed by adding total incurred losses and LAE, including the impact of catastrophe losses, and loss and LAE reserve development from prior years with the Insurance Expense (including write-offs of long-lived assets) Ratio. The Company believes Underlying Losses and LAE and the Underlying Combined Ratio are useful to investors and are used by management to reveal the trends in the Company's Property & Casualty Insurance business that may be obscured by catastrophe losses and prior year reserve development. These catastrophe losses may cause the Company's loss trends to vary significantly between periods as a result of their incidence of occurrence and magnitude, and can have a significant impact on incurred losses and LAE and the combined ratio. Prior-year reserve developments are caused by unexpected loss development on historical reserves. Because reserve development relates to the re-estimation of losses from earlier periods, it has no bearing on the performance of the Company's insurance products in the current period. The Company believes it is useful for investors to evaluate these components separately and in the aggregate when reviewing the Company's underwriting performance.

## Consolidated Net Operating Income

Consolidated Net Operating Income is an after-tax, non-GAAP measure and is computed by excluding from Income from Continuing Operations the after-tax impact of 1) Net Realized Gains on Sales of Investments, 2) Net Impairment Losses Recognized in Earnings related to investments and 3) significant non-recurring or infrequent items that may not be indicative of ongoing operations. Significant non-recurring items are excluded when (a) the nature of the charge or gain is such that it is reasonably unlikely to recur within two years, and (b) there has been no similar charge or gain within the prior two years. The most directly comparable GAAP financial measure is Income from Continuing Operations.

The Company believes that Consolidated Net Operating Income provides investors with a valuable measure of its ongoing performance because it reveals underlying operational performance trends that otherwise might be less apparent if the items were not excluded. Net Realized Gains on Sales of Investments and Net Impairment Losses Recognized in Earnings related to investments included in the Company's results may vary significantly between periods and are generally driven by business decisions and external economic developments such as capital market conditions that impact the values of the Company's investments, the timing of which is unrelated to the insurance underwriting process. Significant non-recurring items are excluded because, by their nature, they are not indicative of the Company's business or economic trends.

A reconciliation of Consolidated Net Operating Income to Income from Continuing Operations for the years ended December 31, 2014, 2013 and 2012 is presented below:

DOLLARS IN MILLIONS	2014	2013	2012
Consolidated Net Operating Income	\$97.1	\$159.2	\$53.8
Net Income (Loss) From:			
Net Realized Gains on Sales of Investments	25.4	64.4	42.5
Net Impairment Losses Recognized in Earnings	(9.9)	(9.1)	(4.5)
Income from Continuing Operations	\$112.6	\$214.5	\$91.8

There were no applicable significant non-recurring items that the Company excluded from the calculation of Consolidated Net Operating Income for the years ended December 31, 2014, 2013 and 2012.

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## PROPERTY &amp; CASUALTY INSURANCE

Selected financial information for the Property &amp; Casualty Insurance segment follows:

DOLLARS IN MILLIONS	2014	2013	2012	
Net Premiums Written	\$1,189.1	\$1,342.2	\$1,454.1	
Earned Premiums	\$1,249.5	\$1,392.9	\$1,467.2	
Net Investment Income	72.7	90.9	77.9	
Other Income	0.5	0.5	0.7	
Total Revenues	1,322.7	1,484.3	1,545.8	
Incurred Losses and LAE related to:				
Current Year:				
Non-catastrophe Losses and LAE	845.2	980.2	1,095.3	
Catastrophe Losses and LAE	96.5	47.1	118.5	
Prior Years:				
Non-catastrophe Losses and LAE	(38.6 )	(45.5 )	(18.5 )	
Catastrophe Losses and LAE	(15.8 )	(12.5 )	(6.4 )	
Total Incurred Losses and LAE	887.3	969.3	1,188.9	
Insurance Expenses, Excluding Write-off of Long-lived Asset	353.7	375.4	392.5	
Write-off of Long-lived Asset	54.6	—	—	
Operating Profit (Loss)	27.1	139.6	(35.6 )	
Income Tax Benefit (Expense)	(2.2 )	(39.0 )	24.7	
Segment Net Operating Income (Loss)	\$24.9	\$100.6	\$(10.9 )	
Ratios Based On Earned Premiums				
Current Year Non-catastrophe Losses and LAE Ratio	67.7	% 70.4	% 74.6	%
Current Year Catastrophe Losses and LAE Ratio	7.7	3.4	8.1	
Prior Years Non-catastrophe Losses and LAE Ratio	(3.1 )	(3.3 )	(1.3 )	
Prior Years Catastrophe Losses and LAE Ratio	(1.3 )	(0.9 )	(0.4 )	
Total Incurred Loss and LAE Ratio	71.0	69.6	81.0	
Insurance Expense Ratio, Excluding Write-off of Long-lived Asset	28.3	27.0	26.8	
Impact on Ratio from Write-off of Long-lived Asset	4.4	—	—	
Combined Ratio	103.7	% 96.6	% 107.8	%
Underlying Combined Ratio				
Current Year Non-catastrophe Losses and LAE Ratio	67.7	% 70.4	% 74.6	%
Insurance Expense Ratio, Excluding Write-off of Long-lived Asset	28.3	27.0	26.8	
Impact on Ratio from Write-off of Long-lived Asset	4.4	—	—	
Underlying Combined Ratio	100.4	% 97.4	% 101.4	%
Non-GAAP Measure Reconciliation				
Underlying Combined Ratio	100.4	% 97.4	% 101.4	%
Current Year Catastrophe Losses and LAE Ratio	7.7	3.4	8.1	
Prior Years Non-catastrophe Losses and LAE Ratio	(3.1 )	(3.3 )	(1.3 )	
Prior Years Catastrophe Losses and LAE Ratio	(1.3 )	(0.9 )	(0.4 )	
Combined Ratio as Reported	103.7	% 96.6	% 107.8	%

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

PROPERTY & CASUALTY INSURANCE (Continued)  
CATASTROPHE FREQUENCY AND SEVERITY

DOLLARS IN MILLIONS	Dec 31, 2014		Dec 31, 2013	
	Number of Events	Losses and LAE	Number of Events	Losses and LAE
Range of Losses and LAE Per Event:				
Below \$5	27	\$30.1	28	\$47.1
\$5 - \$10	3	19.8	—	—
\$10 - \$15	1	12.8	—	—
\$15 - \$20	—	—	—	—
\$20 - \$25	—	—	—	—
Greater Than \$25	1	33.8	—	—
Total	32	\$96.5	28	\$47.1

## INSURANCE RESERVES

DOLLARS IN MILLIONS	Dec 31, 2014	Dec 31, 2013
Insurance Reserves:		
Automobile	\$501.4	\$595.1
Homeowners	102.4	99.9
Other	47.3	47.6
Insurance Reserves	\$651.1	\$742.6
Insurance Reserves:		
Loss Reserves:		
Case	\$423.6	\$471.2
Incurred But Not Reported	135.8	169.0
Total Loss Reserves	559.4	640.2
LAE Reserves	91.7	102.4
Insurance Reserves	\$651.1	\$742.6
Overall		

In the first quarter of 2014, the Company realigned its property and casualty insurance businesses. As a result of the realignment, the property and casualty insurance businesses are being reported as a single business segment named the Property & Casualty Insurance segment. The Company has reclassified certain prior-year amounts in its segment results in the Consolidated Financial Statements to conform to the current year presentation.

See MD&A, "Critical Accounting Estimates," under the caption "Property and Casualty Insurance Reserves for Losses and Loss Adjustment Expenses" beginning on page 53 for additional information pertaining to the Company's process of estimating property and casualty insurance reserves for losses and LAE, development of property and casualty insurance losses and LAE from prior accident years, also referred to as "reserve development" in the discussion of segment results, estimated variability of property and casualty insurance reserves for losses and LAE, and a discussion of some of the variables that may impact development of property and casualty insurance losses and LAE and the estimated variability of property and casualty insurance reserves for losses and LAE.

## 2014 Compared with 2013

Earned Premiums in the Property & Casualty Insurance segment decreased by \$143.4 million, as lower volume accounted for a decrease of \$211.4 million, while higher average premium accounted for an increase of \$68.0 million. The lower volume was driven primarily by personal automobile insurance and homeowners insurance, which had volume decreases of \$167.6 million and \$39.8 million, respectively. The increase in average premium was also driven primarily by personal automobile insurance



## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## PROPERTY &amp; CASUALTY INSURANCE (Continued)

and homeowners insurance, which had increases of \$39.9 million and \$26.0 million, respectively. The decrease in premium volume is on both new business production and retention levels and is due primarily to the rate and resegmentation efforts of the Company in the past few years. The Company has undertaken various actions to improve its retention and new business production, including moderating rate increases in its more recent rate filings due to the improvement in profitability of the book of business.

Net Investment Income in the Property & Casualty Insurance segment decreased by \$18.2 million for the year ended December 31, 2014, compared to 2013, due primarily to lower investment income from Equity Method Limited Liability Investments, lower yields on fixed maturities and lower levels of investments resulting from a decline in the scale of the business. The Property & Casualty Insurance segment reported net investment income from Equity Method Limited Liability Investments of \$8.4 million in 2014, compared to \$16.5 million in 2013.

The Property & Casualty Insurance segment reported Segment Net Operating Income of \$24.9 million for the year ended December 31, 2014, compared to \$100.6 million in 2013. Segment Net Operating Income decreased by \$75.7 million due primarily to the write-off of certain internal use software during the third quarter of 2014, higher incurred catastrophe losses and LAE (excluding reserve development), lower net investment income and higher insurance expenses as a percentage of earned premiums, partially offset by lower underlying losses and LAE as a percentage of earned premiums. See MD&A, "Write-off of Long-lived Asset," on page 48 for more information related to the internal use software write-off. Underlying losses and LAE as a percentage of earned premiums were 67.7% in 2014, a decrease of 2.7 percentage points compared to 2013, as personal automobile insurance, homeowners insurance and commercial automobile insurance improved, while other personal insurance deteriorated. Underlying losses and LAE exclude the impact of catastrophes and loss and LAE reserve development. Catastrophe losses and LAE (excluding reserve development) were \$96.5 million in 2014, compared to \$47.1 million in 2013, which was an increase of \$49.4 million due primarily to one catastrophe event that exceeded \$25 million of losses and LAE and four other catastrophe events that each exceeded \$5 million of losses and LAE in 2014, compared to no such events in excess of \$5 million in 2013. Favorable loss and LAE reserve development (including catastrophe reserve development) was \$54.4 million in 2014, compared to \$58.0 million in 2013. Insurance expenses, excluding the write-off of the long-lived software asset, decreased by \$21.7 million in 2014, compared to 2013, but increased as a percentage of earned premiums from 27.0% in 2013 to 28.3% in 2014, due primarily to lower earned premiums to absorb fixed costs. The Property & Casualty Insurance segment's effective income tax rate differs from the federal statutory income tax rate due primarily to tax-exempt investment income and dividends received deductions. Tax-exempt investment income and dividends received deductions were \$20.9 million in 2014, compared to \$27.1 million in 2013.

## 2013 Compared with 2012

Earned Premiums in the Property & Casualty Insurance segment decreased by \$74.3 million for the year ended December 31, 2013, compared to 2012. The decrease was driven primarily by personal automobile insurance, which decreased by \$91.0 million.

Net Investment Income in the Property & Casualty Insurance segment increased by \$13.0 million for the year ended December 31, 2013, compared to 2012, due primarily to higher net investment income from Equity Method Limited Liability Investments and higher dividends on equity securities, partially offset by lower yields on fixed maturities. The Property & Casualty Insurance segment reported net investment income from Equity Method Limited Liability Investments of \$16.5 million in 2013, compared to \$7.0 million in 2012.

The Property & Casualty Insurance segment reported Segment Net Operating Income of \$100.6 million for the year ended December 31, 2013, compared to Segment Net Operating Loss of \$10.9 million in 2012. Segment net operating results improved by \$111.5 million due primarily to lower incurred catastrophe losses and LAE (excluding reserve development), lower underlying losses and LAE as a percentage of earned premiums, a higher level of favorable loss and LAE reserve development and higher net investment income. Underlying losses and LAE as a percentage of earned premiums were 70.4% in 2013, a decrease of 4.2% percentage points compared to 2012, as personal automobile insurance, homeowners insurance and other personal insurance improved, while commercial automobile



insurance deteriorated. Catastrophe losses and LAE (excluding reserve development) were \$47.1 million in 2013, compared to \$118.5 million in 2012, which was a decrease of \$71.4 million. See MD&A, "Catastrophes," beginning on page 28 for more information on catastrophic events and catastrophe losses and LAE. Favorable loss and LAE reserve development (including catastrophe reserve development) was \$58.0 million in 2013, compared to \$24.9 million in 2012. Insurance expenses decreased by \$17.1 million in 2013 compared to 2012 but were

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## PROPERTY &amp; CASUALTY INSURANCE (Continued)

fairly flat as a percentage of earned premiums. The Property & Casualty Insurance segment's effective income tax rate differs from the federal statutory income tax rate due primarily to tax-exempt investment income and dividends received deductions. Tax-exempt investment income and dividends received deductions were \$27.1 million in 2013, compared to \$34.9 million in 2012.

## Personal Automobile Insurance

Selected financial information for the personal automobile insurance product line follows.

DOLLARS IN MILLIONS	2014	2013	2012		
Net Premiums Written	\$789.0	\$914.2	\$1,025.1		
Earned Premiums	\$831.4	\$959.1	\$1,050.1		
Incurred Losses and LAE related to:					
Current Year:					
Non-catastrophe Losses and LAE	\$616.0	\$741.7	\$839.6		
Catastrophe Losses and LAE	12.7	7.6	23.1		
Prior Years:					
Non-catastrophe Losses and LAE	(31.0 )	(29.9 )	2.1		
Catastrophe Losses and LAE	(0.6 )	(0.2 )	—		
Total Incurred Losses and LAE	\$597.1	\$719.2	\$864.8		
Ratios Based On Earned Premiums					
Current Year Non-catastrophe Losses and LAE Ratio	74.1	% 77.3	% 80.0		%
Current Year Catastrophe Losses and LAE Ratio	1.5	0.8	2.2		
Prior Years Non-catastrophe Losses and LAE Ratio	(3.7 )	(3.1 )	0.2		
Prior Years Catastrophe Losses and LAE Ratio	(0.1 )	—	—		
Total Incurred Loss and LAE Ratio	71.8	% 75.0	% 82.4		%

## 2014 Compared with 2013

Earned premiums on personal automobile insurance decreased by \$127.7 million as lower volume accounted for a decrease of \$167.6 million, while higher average premium accounted for an increase of \$39.9 million. The run-off of the direct-to-consumer business accounted for approximately 20% of the decrease in earned premiums attributed to lower volume. Incurred losses and LAE were \$597.1 million, or 71.8% of earned premiums, in 2014, compared to \$719.2 million, or 75.0% of earned premiums, in 2013. Incurred losses and LAE as a percentage of earned premiums decreased due to lower underlying losses and LAE as a percentage of earned premiums and a higher level of favorable loss and LAE reserve development, partially offset by higher incurred catastrophe losses and LAE (excluding reserve development). Underlying losses and LAE as a percentage of earned premiums were 74.1% in 2014, compared to 77.3% in 2013, which is an improvement of 3.2 percentage points due primarily to the impact of pricing and underwriting actions taken by the Company, lower severity of bodily injury losses and lower frequency of claims across most liability coverages, partially offset by higher severity of losses on most coverages except bodily injury. Catastrophe losses and LAE (excluding reserve development) were \$12.7 million in 2014, compared to \$7.6 million in 2013. Favorable loss and LAE reserve development was \$31.6 million in 2014, compared to \$30.1 million in 2013.

## 2013 Compared with 2012

Earned premiums on personal automobile insurance decreased by \$91.0 million as lower volume accounted for a decrease of \$139.8 million, while higher average premium accounted for an increase of \$48.8 million. The run-off of the direct-to-consumer business accounted for approximately 37% of the decrease in earned premiums attributed to lower volume. Incurred losses and LAE were \$719.2 million, or 75.0% of earned premiums, in 2013, compared to \$864.8 million, or 82.4% of earned premiums, in 2012. Incurred losses and LAE as a percentage of earned premiums decreased due to a favorable impact from a change in loss and LAE reserve development, lower underlying losses and LAE as a percentage of earned premiums and lower incurred catastrophe losses and LAE (excluding reserve development). Underlying losses and LAE as a percentage of earned



## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## PROPERTY &amp; CASUALTY INSURANCE (Continued)

premiums were 77.3% in 2013, compared to 80.0% in 2012, which is an improvement of 2.7 percentage points due primarily to the impact of rate actions taken by the Company on average premium and lower frequency of claims across most coverages, particularly bodily injury, partially offset by higher severity of losses on most other coverages, particularly physical damage. Catastrophe losses and LAE (excluding reserve development) were \$7.6 million in 2013, compared to \$23.1 million in 2012.

Favorable loss and LAE reserve development was \$30.1 million in 2013, compared to adverse loss and LAE reserve development of \$2.1 million in 2012.

## Homeowners Insurance

Selected financial information for the homeowners insurance product line follows.

DOLLARS IN MILLIONS	2014	2013	2012
Net Premiums Written	\$296.5	\$320.9	\$325.3
Earned Premiums	\$312.4	\$326.2	\$318.0
Incurred Losses and LAE related to:			
Current Year:			
Non-catastrophe Losses and LAE	\$156.5	\$170.4	\$191.7
Catastrophe Losses and LAE	80.8	38.2	90.4
Prior Years:			
Non-catastrophe Losses and LAE	(1.5 )	(8.9 )	(5.6 )
Catastrophe Losses and LAE	(13.3 )	(11.2 )	(6.1 )
Total Incurred Losses and LAE	\$222.5	\$188.5	\$270.4
Ratios Based On Earned Premiums			
Current Year Non-catastrophe Losses and LAE Ratio	50.1 %	52.2 %	60.3 %
Current Year Catastrophe Losses and LAE Ratio	25.9	11.7	28.4
Prior Years Non-catastrophe Losses and LAE Ratio	(0.5 )	(2.7 )	(1.8 )
Prior Years Catastrophe Losses and LAE Ratio	(4.3 )	(3.4 )	(1.9 )
Total Incurred Loss and LAE Ratio	71.2 %	57.8 %	85.0 %

## 2014 Compared with 2013

Earned premiums in homeowners insurance decreased by \$13.8 million as lower volume accounted for a decrease of \$39.8 million, while higher average premium accounted for an increase of \$26.0 million. Incurred losses and LAE were \$222.5 million, or 71.2% of earned premiums, in 2014, compared to \$188.5 million, or 57.8% of earned premiums, in 2013. Incurred losses and LAE as a percentage of earned premiums increased due to higher incurred catastrophe losses and LAE (excluding reserve development) and a lower level of favorable loss and LAE reserve development, partially offset by lower underlying losses and LAE as a percentage of earned premiums. Underlying losses and LAE as a percentage of earned premiums were 50.1% in 2014, compared to 52.2% in 2013, which is an improvement of 2.1 percentage points due primarily to the impact of pricing and underwriting actions taken by the Company, partially offset by higher frequency of claims and higher severity of losses. Catastrophe losses and LAE (excluding reserve development) were \$80.8 million in 2014, compared to \$38.2 million in 2013. Favorable loss and LAE reserve development was \$14.8 million in 2014, compared to \$20.1 million in 2013.

## 2013 Compared with 2012

Earned premiums in homeowners insurance increased by \$8.2 million as higher average premium accounted for an increase of \$27.5 million, while lower volume accounted for a decrease of \$19.3 million. Incurred losses and LAE were \$188.5 million, or 57.8% of earned premiums, in 2013, compared to \$270.4 million, or 85.0% of earned premiums, in 2012. Incurred losses and LAE as a percentage of earned premiums decreased due to lower incurred catastrophe losses and LAE (excluding reserve development), lower underlying losses and LAE as a percentage of earned premiums and a higher level of favorable loss and LAE reserve development. Underlying losses and LAE as a percentage of earned premiums were 52.2% in 2013, compared to 60.3% in 2012, which is an improvement of 8.1

percentage points due primarily to lower severity of losses and the impact of

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## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## PROPERTY &amp; CASUALTY INSURANCE (Continued)

rate actions taken by the Company on average premium. Catastrophe losses and LAE (excluding reserve development) were \$38.2 million in 2013, compared to \$90.4 million in 2012. Favorable loss and LAE reserve development was \$20.1 million in 2013, compared to \$11.7 million in 2012.

## Commercial Automobile Insurance

Selected financial information for the commercial automobile insurance product line follows.

DOLLARS IN MILLIONS	2014	2013	2012	
Net Premiums Written	\$55.6	\$53.7	\$48.2	
Earned Premiums	\$54.8	\$52.3	\$43.5	
Incurred Losses and LAE related to:				
Current Year:				
Non-catastrophe Losses and LAE	\$44.6	\$43.7	\$35.4	
Catastrophe Losses and LAE	0.2	0.1	0.1	
Prior Years:				
Non-catastrophe Losses and LAE	(2.6 )	(3.0 )	(12.6 )	
Catastrophe Losses and LAE	—	—	—	
Total Incurred Losses and LAE	\$42.2	\$40.8	\$22.9	
Ratios Based On Earned Premiums				
Current Year Non-catastrophe Losses and LAE Ratio	81.3	% 83.5	% 81.4	%
Current Year Catastrophe Losses and LAE Ratio	0.4	0.2	0.2	
Prior Years Non-catastrophe Losses and LAE Ratio	(4.7 )	(5.7 )	(29.0 )	
Prior Years Catastrophe Losses and LAE Ratio	—	—	—	
Total Incurred Loss and LAE Ratio	77.0	% 78.0	% 52.6	%

## 2014 Compared with 2013

Earned premiums in commercial automobile insurance increased by \$2.5 million due to higher volume with average premium remaining consistent. Incurred losses and LAE were \$42.2 million, or 77.0% of earned premiums, in 2014, compared to \$40.8 million, or 78.0% of earned premiums, in 2013. Incurred losses and LAE as a percentage of earned premiums decreased due to lower underlying losses and LAE as a percentage of earned premiums, partially offset by a lower level of favorable loss and LAE reserve development. Underlying losses and LAE as a percentage of earned premiums were 81.3% in 2014, compared to 83.5% in 2013, which is an improvement of 2.2 percentage points due primarily to lower severity of losses across most coverages, partially offset by higher frequency of claims across most coverages. Favorable loss and LAE reserve development was \$2.6 million in 2014, compared to \$3.0 million in 2013.

## 2013 Compared with 2012

Earned premiums in commercial automobile insurance increased by \$8.8 million as higher volume accounted for an increase of \$8.2 million, while higher average premium accounted for an increase of \$0.6 million. Incurred losses and LAE were \$40.8 million, or 78.0% of earned premiums, in 2013, compared to \$22.9 million, or 52.6% of earned premiums, in 2012. Incurred losses and LAE as a percentage of earned premiums increased due primarily to a lower level of favorable loss and LAE reserve development and higher underlying losses and LAE as a percentage of earned premiums. Underlying losses and LAE as a percentage of earned premiums were 83.5% in 2013, compared to 81.4% in 2012, which is an increase of 2.1 percentage points due primarily to higher severity of losses and, to a lesser extent, higher frequency of claims, partially offset by the positive impact of rate actions taken by the Company on average premium. Favorable loss and LAE reserve development was \$3.0 million in 2013, compared to \$12.6 million in 2012.

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## PROPERTY &amp; CASUALTY INSURANCE (Continued)

## Other Personal Insurance

Other personal insurance products include umbrella, dwelling fire, inland marine, earthquake, boatowners and other liability coverages. Selected financial information for other personal insurance product lines follows.

DOLLARS IN MILLIONS	2014	2013	2012	
Net Premiums Written	\$48.0	\$53.4	\$55.5	
Earned Premiums	\$50.9	\$55.3	\$55.6	
Incurred Losses and LAE related to:				
Current Year:				
Non-catastrophe Losses and LAE	\$28.1	\$24.4	\$28.6	
Catastrophe Losses and LAE	2.8	1.2	4.9	
Prior Years:				
Non-catastrophe Losses and LAE	(3.5 )	(3.7 )	(2.4 )	
Catastrophe Losses and LAE	(1.9 )	(1.1 )	(0.3 )	
Total Incurred Losses and LAE	\$25.5	\$20.8	\$30.8	
Ratios Based On Earned Premiums				
Current Year Non-catastrophe Losses and LAE Ratio	55.2	% 44.1	% 51.4	%
Current Year Catastrophe Losses and LAE Ratio	5.5	2.2	8.8	
Prior Years Non-catastrophe Losses and LAE Ratio	(6.9 )	(6.7 )	(4.3 )	
Prior Years Catastrophe Losses and LAE Ratio	(3.7 )	(2.0 )	(0.5 )	
Total Incurred Loss and LAE Ratio	50.1	% 37.6	% 55.4	%

## 2014 Compared with 2013

Earned premiums in other personal insurance decreased by \$4.4 million as lower volume accounted for a decrease of \$6.6 million, while higher average premium accounted for an increase of \$2.2 million. Incurred losses and LAE were \$25.5 million, or 50.1% of earned premiums, in 2014, compared to \$20.8 million, or 37.6% of earned premiums, in 2013. Incurred losses and LAE as a percentage of earned premiums increased due to higher underlying losses and LAE as a percentage of earned premiums and higher catastrophe losses and LAE (excluding reserve development), partially offset by a higher level of favorable loss and LAE reserve development. Underlying losses and LAE as a percentage of earned premiums were 55.2% in 2014, compared to 44.1% in 2013, which is an increase of 11.1 percentage points due primarily to higher severity of losses and frequency of claims across most coverages.

Catastrophe losses and LAE (excluding reserve development) were \$2.8 million in 2014, compared to \$1.2 million in 2013. Favorable loss and LAE reserve development was \$5.4 million in 2014, compared to \$4.8 million in 2013.

## 2013 Compared with 2012

Earned premiums in other personal insurance decreased by \$0.3 million as lower volume accounted for a decrease of \$2.4 million, while higher average premium accounted for an increase of \$2.1 million. Incurred losses and LAE were \$20.8 million, or 37.6% of earned premiums, in 2013, compared to \$30.8 million, or 55.4% of earned premiums, in 2012. Incurred losses and LAE as a percentage of earned premiums decreased due to lower underlying losses and LAE as a percentage of earned premiums, lower catastrophe losses and LAE (excluding reserve development) and a higher level of favorable loss and LAE reserve development. Underlying losses and LAE as a percentage of earned premiums were 44.1% in 2013, compared to 51.4% in 2012, which is a decrease of 7.3 percentage points due primarily to lower frequency of umbrella liability insurance claims, lower severity of losses in other insurance lines (excluding umbrella liability) and higher average premium, partially offset by higher severity of umbrella liability insurance losses. Catastrophe losses and LAE (excluding reserve development) were \$1.2 million in 2013, compared to \$4.9 million in 2012. Favorable loss and LAE reserve development was \$4.8 million in 2013, compared to \$2.7 million in 2012.





## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## LIFE &amp; HEALTH INSURANCE

Selected financial information for the Life &amp; Health Insurance segment follows:

DOLLARS IN MILLIONS	2014	2013	2012
Earned Premiums:			
Life	\$387.6	\$392.7	\$393.4
Accident and Health	148.6	161.4	165.2
Property	76.5	78.8	81.3
Total Earned Premiums	612.7	632.9	639.9
Net Investment Income	218.7	209.9	204.3
Other Income	0.9	0.2	0.1
Total Revenues	832.3	843.0	844.3
Policyholders' Benefits and Incurred Losses and LAE	374.4	387.9	393.1
Insurance Expenses	316.0	318.2	310.8
Operating Profit	141.9	136.9	140.4
Income Tax Expense	(50.1 )	(47.6 )	(49.6 )
Segment Net Operating Income	\$91.8	\$89.3	\$90.8

## INSURANCE RESERVES

DOLLARS IN MILLIONS	Dec 31, 2014	Dec 31, 2013
Insurance Reserves:		
Future Policyholder Benefits	\$3,214.7	\$3,157.7
Incurred Losses and LAE Reserves:		
Life	38.8	37.6
Accident and Health	20.2	22.2
Property	4.5	5.3
Total Incurred Losses and LAE Reserves	63.5	65.1
Insurance Reserves	\$3,278.2	\$3,222.8

## 2014 Compared with 2013

Earned Premiums in the Life & Health Insurance segment decreased by \$20.2 million for the year ended December 31, 2014, compared to 2013. Earned premiums on life insurance decreased by \$5.1 million in 2014, compared to 2013, due primarily to a lower volume of insurance, as a decrease of \$12.6 million from life insurance products offered by the Kemper Home Service Companies ("KHSC") was partially offset by an increase of \$7.5 million from life insurance products offered by Reserve National. In late 2012, Reserve National began offering its life insurance products through an expanded network of brokers and non-exclusive independent agents (See Item 1A., "Risk Factors" under the title "Reserve National's operating history with its expanded distribution channels and new products is limited.") Earned premiums on accident and health insurance decreased by \$12.8 million in 2014, compared to 2013, due primarily to lower volume of insurance resulting primarily from the run-off of certain health insurance products largely due to the impact of the Health Care Acts, partially offset by higher volume of supplemental health insurance products. Some of the health insurance products previously sold by Reserve National have been adversely impacted by provisions of the Health Care Acts. In particular, provisions, effective in 2014, prohibiting the renewal of certain policies issued by Reserve National after the issuance of the Health Care Acts and also establishing health insurance exchanges, and a provision which sets minimum loss ratios for health insurance policies have adversely impacted Reserve National's business. Such affected health insurance products (the "HCA Affected Products") accounted for \$30.8 million, or 21%, of the Life & Health Insurance segment's accident and health insurance earned premiums in 2014 and \$49.6 million, or 31%, of the Life & Health Insurance segment's accident and health insurance earned premiums in 2013. Reserve National has adapted its business model in response to the Health Care Acts and ceased selling HCA Affected Products at the end of 2011 and transitioned its sales to supplemental health insurance

products that are not expected to be as severely impacted by the Health Care Acts. Reserve National expects earned premiums from HCA Affected Products to decrease by approximately 50% in 2015 and expects an increase in earned premiums from sales of supplemental insurance products to offset much of the decline. Earned premiums on property insurance decreased by \$2.3 million in 2014, compared to 2013, due primarily to lower

#### LIFE & HEALTH INSURANCE (Continued)

volume, partially offset by higher average premium. The Life & Health Insurance segment has been intentionally running off insurance policies providing dwelling coverage (“Dwelling Policies”) to reduce its exposure to catastrophe risks. Over the last several years, the Life & Health Insurance segment has halted new sales of Dwelling Policies in all markets and non-renewed Dwelling Policies in certain geographical, mainly coastal, areas while continuing to renew policies in other geographical areas. Earned premiums from dwelling coverage comprised 22%, 23% and 26% of the Life & Health Insurance segment’s earned premiums on property insurance in 2014, 2013 and 2012, respectively. Net Investment Income increased by \$8.8 million for the year ended December 31, 2014, compared to 2013, due primarily to higher investment income from other equity interests, partially offset by lower investment income from Equity Method Limited Liability Investments and lower book yields on fixed maturities. Investment income from other equity interests in 2014 included dividend income of \$21.4 million from one company that had sold substantially all of its operations. Net investment loss from Equity Method Limited Liability Investments was \$0.4 million in 2014, compared to net investment income of \$8.4 million in 2013. The weighted-average book yield on the Company’s life and health insurance subsidiaries’ investments in fixed maturities was approximately 5.7% at both December 31, 2014 and December 31, 2013. A protracted low interest rate environment could adversely impact the weighted-average book yield on these subsidiaries’ investments in fixed maturities. For example, the weighted-average book yield on the subsidiaries’ investments in fixed maturities will decline if new money is invested at yields below the portfolio rate. Also, the weighted-average book yield on the subsidiaries’ investments in fixed maturities will decline, to the extent that investments maturing over the next five years are not used for such purposes as paying claims and expenses, if the reinvested portion is at a yield that is lower than the book yield of the maturing investment. The subsidiaries’ investments in fixed maturities that are maturing over the next five years totaled \$574 million at December 31, 2014. The weighted-average book yield on such investments was 7.8% at December 31, 2014. The reinvestment rate for the subsidiaries’ investments in fixed maturities was approximately 7.4% in 2014 with an average duration of 4.8 years at December 31, 2014.

Operating Profit in the Life & Health Insurance segment was \$141.9 million before taxes for the year ended December 31, 2014, compared to \$136.9 million in 2013. Policyholders’ Benefits and Incurred Losses and LAE decreased by \$13.5 million in 2014 due primarily to lower incurred accident and health insurance losses, lower underlying losses on property insurance, lower catastrophe losses and LAE and lower policyholders’ benefits on life insurance, partially offset by an unfavorable impact of property insurance reserve development. Incurred accident and health insurance losses were \$81.1 million, or 54.6% of accident and health insurance earned premiums, in 2014, compared to \$90.9 million, or 56.3% of accident and health insurance earned premiums, in 2013. Incurred accident and health insurance losses as a percentage of accident and health insurance earned premiums decreased due primarily to a change in business mix from the aforementioned run-off of certain health insurance products. Incurred losses and LAE on property insurance were \$24.6 million, or 32.2% of property insurance earned premiums, in 2014, compared to \$27.4 million, or 34.8% of property insurance earned premiums, in 2013. Underlying losses and LAE on property insurance were \$21.7 million, or 28.4% of property insurance earned premiums, in 2014, compared to \$25.6 million, or 32.5% of property insurance earned premiums, in 2013 and decreased due primarily to lower frequency and severity of insurance losses. Catastrophe losses and LAE (excluding reserve development) were \$2.0 million in 2014, compared to \$3.6 million in 2013. Unfavorable loss and LAE reserve development was \$0.9 million in 2014, compared to favorable loss and LAE reserve development of \$1.8 million in 2013. Favorable loss and LAE reserve development in 2013 resulted primarily from a final assessment issued by the MWUA that reduced KHSC’s share of MWUA’s losses for the 2004 through 2006 policy periods by \$2.0 million. Policyholders’ benefits on life insurance were \$268.7 million in 2014, compared to \$269.6 million in 2013, which is a decrease of \$0.9 million due primarily to a lower provision for future policyholders’ benefits and lower death claims related to insurance policies issued by KHSC, partially offset by the higher volume of insurance from policies issued by Reserve National. Insurance Expenses in the Life & Health Insurance segment decreased by \$2.2 million in 2014, compared to 2013, due primarily to lower non-deferrable career agent incentive compensation and service commissions, lower legal costs and lower

salary expense from the capitalization of certain salaries in connection with an internal use software project, partially offset by higher commissions and other expenses resulting from the expansion of Reserve National's distribution channels. Segment Net Operating Income in the Life & Health Insurance segment was \$91.8 million for the year ended December 31, 2014, compared to \$89.3 million in 2013.

2013 Compared with 2012

Earned Premiums in the Life & Health Insurance segment decreased by \$7.0 million for the year ended December 31, 2013, compared to 2012. Earned premiums on life insurance decreased by \$0.7 million in 2013, compared to 2012, due primarily to a

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## LIFE &amp; HEALTH INSURANCE (Continued)

lower volume of insurance, as a decrease of \$6.4 million from life insurance products offered by KHSC was partially offset by an increase of \$5.7 million from life insurance products offered by Reserve National. Earned premiums on accident and health insurance decreased by \$3.8 million in 2013, compared to 2012, due primarily to lower volume of insurance resulting primarily from the run-off of certain health insurance products largely due to the impact of the Health Care Acts, partially offset by higher volume of supplemental health insurance products and higher average premium. HCA Affected Products accounted for \$49.6 million, or 31%, of the Life & Health Insurance segment's accident and health insurance earned premiums in 2013 and \$62.5 million, or 38%, of the Life & Health Insurance segment's accident and health insurance earned premiums in 2012. Earned premiums on property insurance decreased by \$2.5 million in 2013, compared to 2012, due primarily to lower volume of insurance from the run-off and, in certain geographical areas, the non-renewal of Dwelling Policies, partially offset by the impact of non-renewing the Life & Health Insurance segment's catastrophe reinsurance program. Catastrophe reinsurance premiums reduced earned premiums by \$2.0 million for the year ended December 31, 2012 with no such reduction in 2013. Given the actions taken by KHSC to reduce its exposures to catastrophes and except for catastrophe reinsurance provided by the FHCF, KHSC did not renew its catastrophe reinsurance program in 2013.

Net Investment Income increased by \$5.6 million for the year ended December 31, 2013, compared to 2012, due primarily to a higher level of investments in fixed maturities, higher investment income from Equity Method Limited Liability Investments and higher dividends on equity securities, partially offset by lower book yields on fixed maturities. Net investment income from Equity Method Limited Liability Investments was \$8.4 million for the year ended December 31, 2013, compared to \$1.8 million in 2012.

Operating Profit in the Life & Health Insurance segment was \$136.9 million before taxes for the year ended December 31, 2013, compared to \$140.4 million in 2012. Policyholders' Benefits and Incurred Losses and LAE decreased by \$5.2 million in 2013 due primarily to lower underlying losses on property insurance, lower catastrophe losses and LAE and higher favorable loss and LAE reserve development, partially offset by higher policyholders' benefits on life insurance and higher incurred accident and health insurance losses. Incurred losses and LAE on property insurance were \$27.4 million, or 34.8% of property insurance earned premiums, in 2013, compared to \$38.9 million, or 47.8% of property insurance earned premiums, in 2012. Underlying losses and LAE on property insurance were \$25.6 million, or 32.5% of property insurance earned premiums, in 2013, compared to \$33.2 million, or 40.8% of property insurance earned premiums, in 2012 and decreased due primarily to lower severity of insurance losses. Catastrophe losses and LAE (excluding reserve development) were \$3.6 million in 2013, compared to \$6.0 million in 2012.

Favorable loss and LAE reserve development was \$1.8 million in 2013, compared to \$0.3 million in 2012. Favorable loss and LAE reserve development in 2013 resulted primarily from a final assessment issued by the MWUA that reduced KHSC's share of MWUA's losses for the 2004 through 2006 policy periods by \$2.0 million. Policyholders' benefits on life insurance were \$269.6 million in 2013, compared to \$265.3 million in 2012, an increase of \$4.3 million. Policyholders' benefits on life insurance increased due primarily to higher volume of insurance from policies issued by Reserve National and slightly higher mortality rates related to insurance policies issued by KHSC, partially offset by the impact of a higher lapse rate for KHSC's in-force book of business. Incurred accident and health insurance losses were \$90.9 million, or 56.3% of accident and health insurance earned premiums, in 2013, compared to \$88.9 million, or 53.8% of accident and health insurance earned premiums, in 2012. Incurred accident and health insurance losses as a percentage of accident and health insurance earned premiums increased due primarily to higher severity of accident and health insurance losses, partially offset by lower frequency of claims. Insurance Expenses in the Life & Health Insurance segment increased by \$7.4 million in 2013, compared to 2012, due primarily to higher legal costs and start-up expenses to expand Reserve National's distribution channels, partially offset by lower commissions.

Segment Net Operating Income in the Life & Health Insurance segment was \$89.3 million for the year ended December 31, 2013, compared to \$90.8 million in 2012.

Unclaimed Property

Certain state insurance regulators, legislators and treasurers/controllers are involved in an array of initiatives that could result in significant changes to the application of unclaimed property laws and related claims handling practices with respect to life insurance policies. These initiatives seek, in various ways, to impose a new duty on the part of life insurers to proactively search for deaths of their insureds. It is the Company's position that state officials lack the legal authority to impose new requirements where such requirements have the effect of changing the terms of existing life insurance contracts. See Item 1A., "Risk Factors," under the caption "Unclaimed Property Risk Factor," MD&A, "Liquidity and Capital Resources," and Note 22, "Contingencies," to the Consolidated Financial Statements for additional information about these matters.

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## INVESTMENT RESULTS

## Net Investment Income

Net Investment Income for the years ended December 31, 2014, 2013 and 2012 was:

DOLLARS IN MILLIONS	2014	2013	2012
Investment Income (Loss):			
Interest and Dividends on Fixed Maturities	\$227.4	\$235.5	\$246.1
Dividends on Equity Securities	59.9	38.0	25.7
Equity Method Limited Liability Investments	9.0	26.4	9.3
Fair Value Option Investments	(0.7)	—	—
Short-term Investments	0.6	0.1	0.2
Loans to Policyholders	20.5	19.8	18.9
Real Estate	12.1	20.8	27.4
Other	0.1	—	0.1
Total Investment Income	328.9	340.6	327.7
Investment Expenses:			
Real Estate	11.3	18.3	26.1
Other Investment Expenses	8.5	7.6	5.7
Total Investment Expenses	19.8	25.9	31.8
Net Investment Income	\$309.1	\$314.7	\$295.9

## 2014 Compared with 2013

Net Investment Income decreased by \$5.6 million for the year ended December 31, 2014, compared to 2013, due primarily to lower income on Equity Method Limited Liability Investments and lower Interest and Dividends on Fixed Maturities, partially offset by higher dividends on Equity Securities. Investment income from Equity Method Limited Liability Investments decreased by \$17.4 million due to lower investment returns. Interest and Dividends on Fixed Maturities decreased by \$8.1 million due primarily to lower yields and, to a lesser extent, lower levels of Fixed Maturities. Dividends on Equity Securities in 2014 included dividend income of \$21.8 million from one company that had sold substantially all of its operations. Interest income from loans to policyholders increased by \$0.7 million in 2014, compared to 2013, due to a higher level of loans outstanding. Net investment income from real estate decreased by \$1.7 million in 2014, compared to 2013, due primarily to income from the early termination of one tenant's lease in 2013.

## 2013 Compared with 2012

Net Investment Income increased by \$18.8 million for the year ended December 31, 2013, compared to 2012, due primarily to higher income on Equity Method Limited Liability Investments, higher dividends on Equity Securities, higher levels of Fixed Maturities, partially offset by lower yields on Fixed Maturities. Interest income from loans to policyholders increased by \$0.9 million in 2013, compared to 2012, due to a higher level of loans outstanding. Net investment income from real estate increased by \$1.2 million in 2013, compared to 2012, due primarily to income from the early termination of one tenant's lease in 2013.

## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## INVESTMENT RESULTS (Continued)

## Net Realized Gains on Sales of Investments

The components of Net Realized Gains on Sales of Investments for the years ended December 31, 2014, 2013 and 2012 were:

DOLLARS IN MILLIONS	2014	2013	2012
Fixed Maturities:			
Gains on Sales	\$7.0	\$30.9	\$56.9
Losses on Sales	(0.2 )	(0.4 )	(0.1 )
Equity Securities:			
Gains on Sales	33.1	21.8	8.3
Losses on Sales	(2.0 )	(0.5 )	(0.2 )
Equity Method Limited Liability Investments:			
Gains on Sales	—	2.5	—
Real Estate:			
Gains on Sales	—	44.2	0.2
Losses on Sales	(0.2 )	—	—
Other Investments:			
Gain on Sale of Subsidiary	1.6	—	—
Gains on Sales	—	0.1	—
Losses on Sales	(0.1 )	(0.1 )	—
Trading Securities Net Gains (Losses)	(0.1 )	0.6	0.3
Net Realized Gains on Sales of Investments	\$39.1	\$99.1	\$65.4
Gross Gains on Sales	\$41.7	\$99.5	\$65.4
Gross Losses on Sales	(2.5 )	(1.0 )	(0.3 )
Net Gains (Losses) on Trading Securities	(0.1 )	0.6	0.3
Net Realized Gains on Sales of Investments	\$39.1	\$99.1	\$65.4

## Fixed Maturities

In the first quarter of 2013, the Company sold several corporate bonds and notes in conjunction with a comprehensive review of the prospects of each issuer in the Company's publicly-traded corporate bond portfolio. Net Realized Gains on Sales of Fixed Maturities for the year ended December 31, 2013 include realized gains of \$24.8 million from such sales. In the third quarter of 2012, the Company sold several municipal securities to take advantage of attractive pricing for such securities and for tax planning and other portfolio management purposes. Net Realized Gains on Sales of Fixed Maturities for the year ended December 31, 2012 include realized gains of \$44.9 million from such sales. Other sales activity in 2014, 2013 and 2012 was due to normal portfolio management.

## Equity Securities

In the second half of 2014, the Company sold certain common stocks and other equity interests to reduce a concentration with an external investment manager and to accelerate utilization of net operating loss carryforwards. Net Realized Gains on Sales of Equity Securities for the year ended December 31, 2014 include net realized gains of \$21.6 million from such sales. In the fourth quarter of 2013, the Company sold certain common stocks to accelerate the utilization of net operating loss carryforwards. Net Realized Gains on Sales of Equity Securities for the year ended December 31, 2013 include realized gains of \$19.8 million from such sales. Other sales activity in 2014, 2013 and 2012 was due to normal portfolio management.

## Real Estate

In the third quarter of 2013, the Company sold the building where Kemper's corporate offices are headquartered and recognized a realized gain of \$43.6 million. The sale was part of an effort to reduce the Company's real estate exposure and reduce the real estate portfolio's concentration risk.





## Kemper Corporation and Subsidiaries

## Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

## INVESTMENT RESULTS (Continued)

## Net Impairment Losses Recognized in Earnings

The Company regularly reviews its investment portfolio for factors that may indicate that a decline in the fair value of an investment is other-than-temporary. Losses arising from other-than-temporary declines in fair value are reported in the Consolidated Statements of Income in the period that the declines are determined to be other-than-temporary. Information pertaining to Net Impairment Losses Recognized in Earnings reported in the Consolidated Statements of Income for the years ended December 31, 2014, 2013 and 2012 is presented below.

DOLLARS IN MILLIONS	2014		2013		2012	
	Amount	Number of Issuers/ Properties	Amount	Number of Issuers/ Properties	Amount	Number of Issuers/ Properties
Fixed Maturities	\$(5.7 )	21	\$(10.3 )	5	\$(1.9 )	3
Equity Securities	(7.1 )	22	(3.6 )	11	(1.9 )	8
Real Estate	(2.4 )	1	—	0	(3.1 )	5
Net Impairment Losses Recognized in Earnings	\$(15.2 )	44	\$(13.9 )	16	\$(6.9 )	16

## Fixed Maturities

Net Impairment Losses Recognized in the Consolidated Statement of Income for the year ended December 31, 2014 related to Investments in Fixed Maturities include losses of \$0.4 million due to the Company's intent to sell or requirement to sell bonds of eighteen issuers and credit losses of \$5.3 million from other-than-temporary declines in the fair values of investments in fixed maturities of three issuers. Net Impairment Losses Recognized in the Consolidated Statement of Income for the year ended December 31, 2013 related to Investments in Fixed Maturities include losses of \$0.8 million due to the Company's intent to sell or requirement to sell bonds of two issuers and credit losses of \$9.5 million from other-than-temporary declines in the fair values of investments in fixed maturities of three issuers. Net Impairment Losses Recognized in the Consolidated Statements of Income for the year ended December 31, 2012 related to Investments in Fixed Maturities include losses of \$0.4 million due to the Company's intent to sell bonds of one issuer and credit losses of \$1.5 million from other-than-temporary declines in the fair values of investments in fixed maturities of two issuers.

## Real Estate

In 2014, the Company determined that the book value of one property was not recoverable based on the Company's estimate of the weighted-average, undiscounted cash flows from such property. Accordingly, the Company wrote down the property to its estimated fair value and recognized an impairment loss of \$2.4 million in 2014. In 2012, the Company classified certain investments in real estate as held for sale. In connection with such classification, the Company wrote down five properties to their respective estimated net sales prices and recognized impairment losses of \$3.1 million in 2012.

Kemper Corporation and Subsidiaries

Management's Discussion and Analysis of Financial Condition and Results of Operations—(Continued)

INVESTMENT RESULTS (Continued)

Total Comprehensive Investment Gains (Losses)

Total Comprehensive Investment Gains (Losses) are comprised of Net Realized Gains on Sales of Investments and Net Impairment Losses Recognized in Earnings reported in the Consolidated Statements of Income and unrealized investment gains and losses that are not reported in the Consolidated Statements of Income, but rather are reported in the Consolidated Statements of Comprehensive Income. The components of Total Comprehensive Investment Gains (Losses) for the years ended December 31, 2014, 2013 and 2012 were:

DOLLARS IN MILLIONS	2014	2013	2012
Fixed Maturities:			