

AFLAC INC  
Form 10-Q  
August 05, 2016  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q  
(Mark One)

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

For the quarterly period ended June 30, 2016  
or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-07434  
Aflac Incorporated

(Exact name of registrant as specified in its charter)

Georgia 58-1167100  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1932 Wynnton Road, Columbus, Georgia 31999  
(Address of principal executive offices) (ZIP Code)

706.323.3431

(Registrant's telephone number, including area code)

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

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

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class July 28, 2016  
Common Stock, \$.10 Par Value 409,575,251

Aflac Incorporated and Subsidiaries  
 Quarterly Report on Form 10-Q  
 For the Quarter Ended June 30, 2016  
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

Review by Independent Registered Public Accounting Firm

The June 30, 2016, and 2015, consolidated financial statements included in this filing have been reviewed by KPMG LLP, an independent registered public accounting firm, in accordance with established professional standards and procedures for such a review.

The report of KPMG LLP commenting upon its review is included on the following page.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders  
Aflac Incorporated:

We have reviewed the accompanying consolidated balance sheet of Aflac Incorporated and subsidiaries (the Company) as of June 30, 2016, and the related consolidated statements of earnings, and comprehensive income (loss), for the three-month and six-month periods ended June 30, 2016, and 2015, and the consolidated statements of shareholders' equity and cash flows for the six-month periods ended June 30, 2016 and 2015. These consolidated financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

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

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Aflac Incorporated and subsidiaries as of December 31, 2015, and the related consolidated statements of earnings, comprehensive income (loss), shareholders' equity and cash flows for the year then ended (not presented herein); and in our report dated February 25, 2016, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2015, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ KPMG LLP

Atlanta, Georgia  
August 5, 2016

Aflac Incorporated and Subsidiaries  
Consolidated Statements of Earnings

|   | Three Months Ended |         | Six Months Ended |         |
|---|--------------------|---------|------------------|---------|
|   | June 30,           |         | June 30,         |         |
| (In millions, except for share and per-share amounts - Unaudited)                               | 2016               | 2015    | 2016             | 2015    |
| Revenues:   |                    |         |                  |         |
| Net premiums, principally supplemental health insurance   | \$4,823            | \$4,364 | \$9,425          | \$8,796 |
| Net investment income   | 822                | 777     | 1,623            | 1,559   |
| Realized investment gains (losses):   |                    |         |                  |         |
| Other-than-temporary impairment losses realized   | (33 )              | 0       | (47 )            | (6 )    |
| Sales and redemptions   | 13                 | 92      | 104              | 160     |
| Derivative and other gains (losses)   | (167 )             | 35      | (171 )           | (14 )   |
| Total realized investment gains (losses)  | (187 )             | 127     | (114 )           | 140     |
| Other income (loss)   | (21 )              | 19      | (46 )            | 18      |
| Total revenues  | 5,437              | 5,287   | 10,888           | 10,513  |
| Benefits and expenses:  |                    |         |                  |         |
| Benefits and claims, net  | 3,254              | 2,937   | 6,279            | 5,889   |
| Acquisition and operating expenses:   |                    |         |                  |         |
| Amortization of deferred policy acquisition costs   | 284                | 255     | 576              | 532     |
| Insurance commissions   | 345                | 325     | 678              | 655     |
| Insurance expenses  | 613                | 550     | 1,176            | 1,080   |
| Interest expense  | 66                 | 74      | 131              | 157     |
| Other expenses  | 41                 | 272     | (1) 97           | 313 (1) |
| Total acquisition and operating expenses  | 1,349              | 1,476   | 2,658            | 2,737   |
| Total benefits and expenses   | 4,603              | 4,413   | 8,937            | 8,626   |
| Earnings before income taxes  | 834                | 874     | 1,951            | 1,887   |
| Income taxes  | 286                | 301     | 672              | 651     |
| Net earnings  | \$548              | \$573   | \$1,279          | \$1,236 |
| Net earnings per share:   |                    |         |                  |         |
| Basic   | \$1.33             | \$1.33  | \$3.08           | \$2.84  |
| Diluted   | 1.32               | 1.32    | 3.06             | 2.83    |
| Weighted-average outstanding common shares used in computing earnings per share (In thousands): |                    |         |                  |         |
| Basic   | 411,853            | 431,672 | 415,301          | 434,473 |
| Diluted   | 414,326            | 434,257 | 417,623          | 437,077 |
| Cash dividends per share  | \$.41              | \$.39   | \$.82            | \$.78   |

(1) Includes expense of \$230 for the make-whole payment associated with the early extinguishment of debt  
See the accompanying Notes to the Consolidated Financial Statements.

Aflac Incorporated and Subsidiaries  
 Consolidated Statements of Comprehensive Income (Loss)

| (In millions - Unaudited)   | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |          |
|---|--------------------------------|-----------|------------------------------|----------|
|   | 2016                           | 2015      | 2016                         | 2015     |
| Net earnings  | \$548                          | \$573     | \$1,279                      | \$1,236  |
| Other comprehensive income (loss) before income taxes:  |                                |           |                              |          |
| Unrealized foreign currency translation gains (losses) during period                                      | 899                            | (170 )    | 1,588                        | (161 )   |
| Unrealized gains (losses) on investment securities:   |                                |           |                              |          |
| Unrealized holding gains (losses) on investment securities during period                                  | 2,693                          | (2,458 )  | 5,382                        | (1,865 ) |
| Reclassification adjustment for realized (gains) losses on investment securities included in net earnings | 11                             | (68 )     | (66 )                        | (118 )   |
| Unrealized gains (losses) on derivatives during period  | 8                              | 2         | 11                           | (2 )     |
| Pension liability adjustment during period  | (4 )                           | 1         | (6 )                         | 1        |
| Total other comprehensive income (loss) before income taxes   | 3,607                          | (2,693 )  | 6,909                        | (2,145 ) |
| Income tax expense (benefit) related to items of other comprehensive income (loss)                        | 1,111                          | (868 )    | 2,102                        | (673 )   |
| Other comprehensive income (loss), net of income taxes  | 2,496                          | (1,825 )  | 4,807                        | (1,472 ) |
| Total comprehensive income (loss)   | \$3,044                        | \$(1,252) | \$6,086                      | \$(236 ) |

See the accompanying Notes to the Consolidated Financial Statements.

Aflac Incorporated and Subsidiaries  
Consolidated Balance Sheets

| (In millions)   | June 30,<br>2016<br>(Unaudited) | December 31,<br>2015 |
|---|---------------------------------|----------------------|
| Assets:   |                                 |                      |
| Investments and cash:   |                                 |                      |
| Securities available for sale, at fair value:   |                                 |                      |
| Fixed maturities (amortized cost \$65,121 in 2016 and \$56,903 in 2015)   | \$ 74,793                       | \$ 60,795            |
| Fixed maturities - consolidated variable interest entities (amortized cost \$4,878 in 2016 and \$3,739 in 2015) | 5,493                           | 4,554                |
| Perpetual securities (amortized cost \$1,649 in 2016 and \$1,586 in 2015)                                       | 1,635                           | 1,719                |
| Perpetual securities - consolidated variable interest entities (amortized cost \$267 in 2016 and \$255 in 2015) | 197                             | 228                  |
| Equity securities (cost \$227 in 2016 and \$117 in 2015)  | 256                             | 135                  |
| Equity securities - consolidated variable interest entities (cost \$1,018 in 2016 and \$363 in 2015)            | 941                             | 363                  |
| Securities held to maturity, at amortized cost:   |                                 |                      |
| Fixed maturities (fair value \$48,796 in 2016 and \$37,520 in 2015)   | 38,346                          | 33,459               |
| Other investments   | 622                             | 294                  |
| Cash and cash equivalents   | 3,700                           | 4,350                |
| Total investments and cash  | 125,983                         | 105,897              |
| Receivables   | 758                             | 705                  |
| Accrued investment income   | 806                             | 768                  |
| Deferred policy acquisition costs   | 9,552                           | 8,511                |
| Property and equipment, at cost less accumulated depreciation   | 467                             | 427                  |
| Other <sup>(1)</sup>  | 3,721                           | 1,948                |
| Total assets  | \$ 141,287                      | \$ 118,256           |

<sup>(1)</sup> Includes \$177 in 2016 and \$102 in 2015 of derivatives from consolidated variable interest entities

Prior-year amounts have been adjusted for the adoption of accounting guidance on January 1, 2016 related to debt issuance costs.

See the accompanying Notes to the Consolidated Financial Statements.

(continued)

Aflac Incorporated and Subsidiaries  
Consolidated Balance Sheets (continued)

| (In millions, except for share and per-share amounts)   | June 30,<br>2016<br>(Unaudited) | December 31,<br>2015 |
|---|---------------------------------|----------------------|
| Liabilities and shareholders' equity:   |                                 |                      |
| Liabilities:  |                                 |                      |
| Policy liabilities:   |                                 |                      |
| Future policy benefits  | \$82,611                        | \$ 69,687            |
| Unpaid policy claims  | 4,261                           | 3,802                |
| Unearned premiums   | 8,726                           | 7,857                |
| Other policyholders' funds  | 7,468                           | 6,285                |
| Total policy liabilities  | 103,066                         | 87,631               |
| Income taxes  | 6,714                           | 4,340                |
| Payables for return of cash collateral on loaned securities   | 826                             | 941                  |
| Notes payable   | 5,009                           | 4,971                |
| Other <sup>(2)</sup>  | 3,122                           | 2,665                |
| Total liabilities   | 118,737                         | 100,548              |
| Commitments and contingent liabilities (Note 11)  |                                 |                      |
| Shareholders' equity:   |                                 |                      |
| Common stock of \$.10 par value. In thousands: authorized 1,900,000 shares in 2016 and 2015; issued 670,764 shares in 2016 and 669,723 shares in 2015 | 67                              | 67                   |
| Additional paid-in capital  | 1,905                           | 1,828                |
| Retained earnings   | 24,944                          | 24,007               |
| Accumulated other comprehensive income (loss):  |                                 |                      |
| Unrealized foreign currency translation gains (losses)  | (847 )                          | (2,196 )             |
| Unrealized gains (losses) on investment securities  | 6,441                           | 2,986                |
| Unrealized gains (losses) on derivatives  | (19 )                           | (26 )                |
| Pension liability adjustment  | (143 )                          | (139 )               |
| Treasury stock, at average cost   | (9,798 )                        | (8,819 )             |
| Total shareholders' equity  | 22,550                          | 17,708               |
| Total liabilities and shareholders' equity  | \$141,287                       | \$ 118,256           |

<sup>(2)</sup> Includes \$117 in 2016 and \$293 in 2015 of derivatives from consolidated variable interest entities

Prior-year amounts have been adjusted for the adoption of accounting guidance on January 1, 2016 related to debt issuance costs.

See the accompanying Notes to the Consolidated Financial Statements.



Aflac Incorporated and Subsidiaries  
Consolidated Statements of Shareholders' Equity

| (In millions - Unaudited)  | Six Months Ended |          |
|--|------------------|----------|
|  | June 30,         |          |
|  | 2016             | 2015     |
| Common stock:  |                  |          |
| Balance, beginning of period   | \$67             | \$67     |
| Balance, end of period   | 67               | 67       |
| Additional paid-in capital:  |                  |          |
| Balance, beginning of period   | 1,828            | 1,711    |
| Exercise of stock options  | 25               | 24       |
| Share-based compensation   | 34               | 17       |
| Gain (loss) on treasury stock reissued   | 18               | 20       |
| Balance, end of period   | 1,905            | 1,772    |
| Retained earnings:   |                  |          |
| Balance, beginning of period   | 24,007           | 22,156   |
| Net earnings   | 1,279            | 1,236    |
| Dividends to shareholders  | (342 )           | (340 )   |
| Balance, end of period   | 24,944           | 23,052   |
| Accumulated other comprehensive income (loss):   |                  |          |
| Balance, beginning of period   | 625              | 1,979    |
| Unrealized foreign currency translation gains (losses) during period, net of income taxes                              | 1,349            | (184 )   |
| Unrealized gains (losses) on investment securities during period, net of income taxes and reclassification adjustments | 3,455            | (1,288 ) |
| Unrealized gains (losses) on derivatives during period, net of income taxes  | 7                | (1 )     |
| Pension liability adjustment during period, net of income taxes  | (4 )             | 1        |
| Balance, end of period   | 5,432            | 507      |
| Treasury stock:  |                  |          |
| Balance, beginning of period   | (8,819 )         | (7,566 ) |
| Purchases of treasury stock  | (1,014 )         | (848 )   |
| Cost of shares issued  | 35               | 34       |
| Balance, end of period   | (9,798 )         | (8,380 ) |
| Total shareholders' equity   | \$22,550         | \$17,018 |

See the accompanying Notes to the Consolidated Financial Statements.

Aflac Incorporated and Subsidiaries  
Consolidated Statements of Cash Flows

| (In millions - Unaudited)   | Six Months Ended<br>June 30, |                       |
|---|------------------------------|-----------------------|
|   | 2016                         | 2015                  |
| Cash flows from operating activities:   |                              |                       |
| Net earnings  | \$1,279                      | \$1,236               |
| Adjustments to reconcile net earnings to net cash provided by operating activities: |                              |                       |
| Change in receivables and advance premiums  | 53                           | 1                     |
| Increase in deferred policy acquisition costs                                       | (103 )                       | (87 )                 |
| Increase in policy liabilities  | 1,654                        | 1,714                 |
| Change in income tax liabilities  | (136 )                       | 130                   |
| Realized investment (gains) losses  | 114                          | (140 )                |
| Other, net  | (7 )                         | 249 <sup>(1)</sup>    |
| Net cash provided (used) by operating activities                                    | 2,854                        | 3,103                 |
| Cash flows from investing activities:   |                              |                       |
| Proceeds from investments sold or matured:  |                              |                       |
| Securities available for sale:  |                              |                       |
| Fixed maturities sold   | 675                          | 1,410                 |
| Fixed maturities matured or called  | 612                          | 518                   |
| Perpetual securities matured or called  | 234                          | 348                   |
| Equity securities sold  | 50                           | 1                     |
| Securities held to maturity:  |                              |                       |
| Fixed maturities matured or called  | 736                          | 420                   |
| Costs of investments acquired:  |                              |                       |
| Available-for-sale fixed maturities acquired  | (3,827 )                     | (3,004 )              |
| Equity securities acquired  | (691 )                       | 0                     |
| Other investments, net  | (324 )                       | (31 )                 |
| Settlement of derivatives, net  | 664                          | (2,200 )              |
| Cash received (pledged or returned) as collateral, net                              | (525 )                       | (1,001 )              |
| Other, net  | (33 )                        | (27 )                 |
| Net cash provided (used) by investing activities                                    | (2,429 )                     | (3,566 )              |
| Cash flows from financing activities:   |                              |                       |
| Purchases of treasury stock   | (1,014 )                     | (848 )                |
| Proceeds from borrowings  | 0                            | 998                   |
| Principal payments under debt obligations   | (1 )                         | (850 )                |
| Dividends paid to shareholders  | (330 )                       | (328 )                |
| Change in investment-type contracts, net  | 82                           | 147                   |
| Treasury stock reissued   | 19                           | 20                    |
| Other, net  | (37 )                        | (226 ) <sup>(1)</sup> |
| Net cash provided (used) by financing activities                                    | (1,281 )                     | (1,087 )              |
| Effect of exchange rate changes on cash and cash equivalents                        | 206                          | (5 )                  |
| Net change in cash and cash equivalents   | (650 )                       | (1,555 )              |
| Cash and cash equivalents, beginning of period                                      | 4,350                        | 4,658                 |
| Cash and cash equivalents, end of period  | \$3,700                      | \$3,103               |
| Supplemental disclosures of cash flow information:                                  |                              |                       |
| Income taxes paid   | \$944                        | \$527                 |
| Interest paid   | 101                          | 127                   |
| Noncash interest  | 30                           | 30                    |
| Impairment losses included in realized investment losses                            | 47                           | 6                     |

Noncash financing activities:

|                                   |    |    |
|-----------------------------------|----|----|
| Capital lease obligations         | 2  | 1  |
| Treasury stock issued for:        |    |    |
| Associate stock bonus             | 17 | 18 |
| Shareholder dividend reinvestment | 12 | 12 |
| Share-based compensation grants   | 5  | 4  |

<sup>(1)</sup> Operating activities excludes and financing activities includes a cash outflow of \$230 for the make-whole payment associated with the early extinguishment of debt

See the accompanying Notes to the Consolidated Financial Statements.

Aflac Incorporated and Subsidiaries  
Notes to the Consolidated Financial Statements  
(Interim period data – Unaudited)

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Description of Business

Aflac Incorporated (the Parent Company) and its subsidiaries (collectively, the Company) primarily sell supplemental health and life insurance in the United States and Japan. The Company's insurance business is marketed and administered through American Family Life Assurance Company of Columbus (Aflac), which operates in the United States (Aflac U.S.) and as a branch in Japan (Aflac Japan). American Family Life Assurance Company of New York (Aflac New York) is a wholly owned subsidiary of Aflac. Most of Aflac's policies are individually underwritten and marketed through independent agents. Additionally, Aflac U.S. markets and administers group products through Continental American Insurance Company (CAIC), branded as Aflac Group Insurance. Our insurance operations in the United States and our branch in Japan service the two markets for our insurance business. Aflac Japan's revenues, including realized gains and losses on its investment portfolio, accounted for 75% and 70% of the Company's total revenues in the six-month periods ended June 30, 2016, and 2015, respectively. The percentage of the Company's total assets attributable to Aflac Japan was 85% at June 30, 2016, compared with 83% at December 31, 2015.

### Basis of Presentation

We prepare our financial statements in accordance with U.S. generally accepted accounting principles (GAAP). These principles are established primarily by the Financial Accounting Standards Board (FASB). In these Notes to the Consolidated Financial Statements, references to U.S. GAAP issued by the FASB are derived from the FASB Accounting Standards Codification™ (ASC). The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates when recording transactions resulting from business operations based on currently available information. The most significant items on our balance sheet that involve a greater degree of accounting estimates and actuarial determinations subject to changes in the future are the valuation of investments, deferred policy acquisition costs, liabilities for future policy benefits and unpaid policy claims, and income taxes. These accounting estimates and actuarial determinations are sensitive to market conditions, investment yields, mortality, morbidity, commission and other acquisition expenses, and terminations by policyholders. As additional information becomes available, or actual amounts are determinable, the recorded estimates will be revised and reflected in operating results. Although some variability is inherent in these estimates, we believe the amounts provided are adequate.

The unaudited consolidated financial statements include the accounts of the Parent Company, its subsidiaries and those entities required to be consolidated under applicable accounting standards. All material intercompany accounts and transactions have been eliminated.

In the opinion of management, the accompanying unaudited consolidated financial statements of the Company contain all adjustments, consisting of normal recurring accruals, which are necessary to fairly present the consolidated balance sheets as of June 30, 2016 and December 31, 2015, the consolidated statements of earnings and comprehensive income (loss) for the three- and six-month periods ended June 30, 2016, and 2015, and the consolidated statements of shareholders' equity and cash flows for the six-month periods ended June 30, 2016 and 2015. Results of operations for interim periods are not necessarily indicative of results for the entire year. As a result, these financial statements should be read in conjunction with the financial statements and notes thereto included in our annual report to shareholders for the year ended December 31, 2015.

### New Accounting Pronouncements

Recently Adopted Accounting Pronouncements

Business Combinations - Simplifying the Accounting for Measurement-Period Adjustments: In September 2015, the FASB issued guidance requiring that an acquirer recognize adjustments to estimated amounts that are identified during the measurement period in the reporting period in which the adjustments are determined. In the same period's financial statements, the acquirer is required to record income effects of the adjustments as if the accounting had been completed at the acquisition date. The acquirer is also required to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the estimated amounts had been recognized as of the

acquisition date. We adopted this guidance as of January 1, 2016. The adoption of this guidance did not have a significant impact on our financial position or results of operations.

**Fair Value Measurement - Disclosures for investments in certain entities that calculate net asset value per share (or its equivalent):** In May 2015, the FASB issued updated guidance that removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. The amendments also remove the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using that practical expedient. We adopted this guidance as of January 1, 2016. The adoption of this guidance did not have a significant impact on our financial position, results of operations, or disclosures.

**Interest - Imputation of Interest - Simplifying the presentation of debt issuance costs:** In April 2015, the FASB issued updated guidance to simplify presentation of debt issuance costs. The updated guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by this amendment. In August 2015, the FASB issued updated Securities and Exchange Commission (SEC) Staff guidance pertaining to the presentation of debt issuance costs related to line-of-credit arrangements. The guidance states that an entity may defer and present debt issuance costs as an asset, subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. We retrospectively adopted this guidance as of January 1, 2016. The retrospective adoption of this accounting standard resulted in a \$40 million reduction to notes payable and other assets as of December 31, 2015, the earliest balance sheet date presented in the period of adoption.

**Consolidation - Amendments to the consolidation analysis:** In February 2015, the FASB issued updated guidance that affects evaluation of whether limited partnerships and similar legal entities (limited liability corporations and securitization structures, etc.) are variable interest entities (VIEs), evaluation of whether fees paid to a decision maker or a service provider are a variable interest, and evaluation of the effect of fee arrangements and the effect of related parties on the determination of the primary beneficiary under the VIE model for consolidation. The updated guidance eliminates the presumption that a general partner should consolidate a limited partnership. Limited partnership and similar legal entities that provide partners with either substantive kick-out rights or substantive participating rights over the general partner will now be evaluated under the voting interest model rather than the VIE model for consolidation. In situations where no single party has a controlling financial interest in a VIE, the related party relationships under common control should be considered in their entirety in determining whether that common control group has a controlling financial interest in the VIE. We adopted this guidance as of January 1, 2016. The adoption of this guidance impacted our footnote disclosures, but did not have a significant impact on our financial position or results of operations.

**Derivatives and Hedging - Determining whether the host contract in a hybrid financial instrument issued in the form of a share is more akin to debt or equity:** In November 2014, the FASB issued guidance to clarify how to evaluate the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. The guidance also clarifies that an entity should assess the substance of the relevant terms and features when considering how to weight those terms and features. We adopted this guidance as of January 1, 2016. The adoption of this guidance did not have a significant impact on our financial position or results of operations.

**Compensation - Stock Compensation - Accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period:** In June 2014, the FASB issued this amendment that provides guidance on certain share-based payment awards that require a specific performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition.

A reporting entity should apply existing guidance to awards with performance conditions that affect vesting to account for such awards. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. The total amount of compensation cost recognized during and after the requisite service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. We adopted this guidance as of January 1, 2016. The adoption of this guidance did not have a significant impact on our financial position or results of operations.

#### Accounting Pronouncements Pending Adoption

**Financial Instruments - Measurement of Credit Losses on Financial Instruments:** In June 2016, the FASB issued amendments that require a financial asset (or a group of financial assets) measured on an amortized cost basis to be presented net of an allowance for credit losses in order to reflect the amount expected to be collected on the financial asset(s). The measurement of expected credit losses is amended by replacing the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform about a credit loss. Credit losses on available-for-sale debt securities will continue to be measured in a manner similar to current GAAP. However, the amendments require that credit losses be presented as an allowance rather than as a writedown. Other amendments include changes to the balance sheet presentation and interest income recognition of purchased financial assets with a more-than-insignificant amount of credit deterioration since origination. The amendments are effective for public companies for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Companies may early adopt this guidance as of the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. We are evaluating the impact of adoption of this guidance on our financial position, results of operations and disclosures.

**Compensation - Stock Compensation - Improvements to Employee Share-Based Payment Accounting:** In March 2016, the FASB issued amendments which simplify several aspects for share-based payment award transactions, including income tax consequences, classification of awards as either liability or equities, and classification on the statement of cash flows. The amendments are effective for public companies for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted for any interim or annual period. We are currently evaluating the impact of this guidance on our financial position, results of operations or disclosures.

**Investments - Equity Method and Joint Ventures - Simplifying the Transition to the Equity Method of Accounting:** In March 2016, the FASB issued amendments which eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. Per the amendments, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. The amendments also require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Early adoption is permitted. The adoption of this guidance is not expected to have a significant impact on our financial position or results of operations.

**Derivatives and Hedging - Contingent Put and Call Options in Debt Instruments:** In March 2016, the FASB issued amendments which clarify what steps are required when assessing whether the economic characteristics and risks of call (put) options are clearly and closely related to the economic characteristics and risks of their debt hosts, which is one of the criteria for bifurcating an embedded derivative. Consequently, when a call (put) option is contingently exercisable, an entity does not have to assess whether the event that triggers the ability to exercise a call (put) option is related to interest rates or credit risks. The amendments are effective for public business entities for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The adoption of this guidance is not expected to have a significant impact on our financial position or results of operations.



Derivatives and Hedging - Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships: In March 2016, the FASB issued amendments which clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria remain intact. The amendments are effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The adoption of this guidance is not expected to have a significant impact on our financial position or results of operations.

Leases: In January 2016, the FASB issued updated guidance for accounting for leases. Per the amendments, lessees will be required to recognize all leases on the balance sheet, with the exception of short-term leases. A lease liability will be recorded for the obligation of a lessee to make lease payments arising from a lease. A right-of-use asset,

will be recorded which represents the lessee's right to use, or to control the use of, a specified asset for a lease term. Under the new guidance, lessor accounting is largely unchanged. The amendments are effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. We are currently evaluating the impact of this guidance on our financial position, results of operations or disclosures.

**Financial Instruments - Recognition and Measurement of Financial Assets and Financial Liabilities:** In January 2016, the FASB issued guidance to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The main provisions require that equity investments be measured at fair value with changes recognized in net income; that changes in instrument-specific credit risk for financial liabilities that are measured under the fair value option be recognized in other comprehensive income; and that entities would make the assessment of the ability to realize a deferred tax asset (DTA) related to an available-for-sale (AFS) debt security in combination with the entity's other DTAs. The amendments are effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is not permitted, with the exception of the own credit provision if an entity has elected to measure a liability at fair value. We are evaluating whether the adoption of this guidance will have a significant impact on our financial position, results of operations or disclosures.

**Financial Services - Insurance - Disclosures about Short-Duration Contracts:** In May 2015, the FASB issued updated guidance requiring enhanced disclosures by all insurance entities that issue short-duration contracts. The amendments require insurance entities to disclose for annual reporting periods information about the liability for unpaid claims and claim adjustment expenses. The amendments also require insurance entities to disclose information about significant changes in methodologies and assumptions used to calculate the liability for unpaid claims and claim adjustment expenses. In addition, the amendments require insurance entities to disclose for annual and interim reporting periods a roll-forward of the liability for unpaid claims and claim adjustment expenses. For health insurance claims, the amendments require the disclosure of the total of incurred-but-not-reported liabilities and expected development on reported claims included in the liability for unpaid claims and claim adjustment expenses. The amendments are effective for public business entities for annual periods beginning after December 15, 2015, and interim periods within annual periods beginning after December 15, 2016. Early application of the amendments is permitted. The adoption of this guidance will not have a significant impact on our financial position or results of operations.

**Presentation of Financial Statements - Going Concern - Disclosure of uncertainties about an entity's ability to continue as a going concern:** In August 2014, the FASB issued this amendment that provides U.S. GAAP guidance on management's responsibility in evaluating whether there is substantial doubt about a company's ability to continue as a going concern and about related footnote disclosures. For each reporting period, management will be required to evaluate whether there are conditions or events that raise substantial doubt about a company's ability to continue as a going concern within one year from the date the financial statements are issued. The amendment is effective for annual periods ending after December 15, 2016, and interim periods within annual periods beginning after December 15, 2016. Early application is permitted for annual or interim reporting periods for which the financial statements have not previously been issued. The adoption of this guidance will not have a significant impact on our financial position or results of operations.

**Revenue from contracts with customers:** In May 2014, the FASB issued updated guidance that affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (e.g., insurance contracts or lease contracts). The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB deferred the effective date for this standard to annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Other updates related to the new guidance, which are effective as of the same reporting period,

pertain to identifying performance obligations and licensing, and principal versus agent considerations. Early application is not permitted. We are currently evaluating the impact of this guidance on our financial position, results of operations or disclosures.

Recent accounting guidance not discussed above is not applicable, did not have, or is not expected to have a material impact to our business.

For additional information on new accounting pronouncements and recent accounting guidance and their impact, if any, on our financial position or results of operations, see Note 1 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015.

## 2. BUSINESS SEGMENT INFORMATION

The Company consists of two reportable insurance business segments: Aflac Japan and Aflac U.S., both of which sell supplemental health and life insurance. Operating business segments that are not individually reportable and business activities, including reinsurance retrocession activities, not included in Aflac Japan or Aflac U.S. are included in the "Other business segments" category.

We do not allocate corporate overhead expenses to business segments. Consistent with U.S. GAAP accounting guidance for segment reporting, we evaluate and manage our business segments using a financial performance measure called pretax operating earnings. Our definition of operating earnings includes interest cash flows associated with notes payable and excludes the following items from net earnings on an after-tax basis: realized investment gains/losses (securities transactions, impairments, and the impact of derivative and hedging activities), nonrecurring items and other non-operating income (loss). We then exclude income taxes related to operations to arrive at pretax operating earnings. Information regarding operations by segment follows:

| (In millions)                                     | Three Months Ended June 30, |         | Six Months Ended June 30, |          |
|---|-----------------------------|---------|---------------------------|----------|
|   | 2016                        | 2015    | 2016                      | 2015     |
| Revenues:   |                             |         |                           |          |
| Aflac Japan:                                      |                             |         |                           |          |
| Net earned premiums                               | \$3,402                     | \$2,978 | \$6,581                   | \$6,056  |
| Net investment income                             | 642                         | 605     | 1,264                     | 1,218    |
| Other income                                      | 11                          | 7       | 19                        | 15       |
| Total Aflac Japan                                 | 4,055                       | 3,590   | 7,864                     | 7,289    |
| Aflac U.S.:                                       |                             |         |                           |          |
| Net earned premiums                               | 1,362                       | 1,331   | 2,729                     | 2,670    |
| Net investment income                             | 176                         | 168     | 350                       | 334      |
| Other income                                      | 0                           | 2       | 3                         | 5        |
| Total Aflac U.S.                                  | 1,538                       | 1,501   | 3,082                     | 3,009    |
| Other business segments                           | 68                          | 65      | 136                       | 91       |
| Total business segment revenues                   | 5,661                       | 5,156   | 11,082                    | 10,389   |
| Realized investment gains (losses) <sup>(1)</sup> | (208 )                      | 104     | (157 )                    | 100      |
| Corporate   | 69                          | 71      | 136                       | 169      |
| Intercompany eliminations                         | (48 )                       | (50 )   | (93 )                     | (133 )   |
| Other non-operating income (loss)                 | (37 )                       | 6       | (80 )                     | (12 )    |
| Total revenues                                    | \$5,437                     | \$5,287 | \$10,888                  | \$10,513 |

<sup>(1)</sup> Excluding a gain of \$21 and \$23 for the three-month periods and \$43 and \$40 for the six-month periods ended June 30, 2016, and 2015, respectively, related to the interest rate component of the change in fair value of foreign currency swaps on notes payable which is classified as an operating gain when analyzing segment operations

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| (In millions)  | Three<br>Months<br>Ended<br>June 30, |        | Six Months<br>Ended<br>June 30, |         |
|--|--------------------------------------|--------|---------------------------------|---------|
|  | 2016                                 | 2015   | 2016                            | 2015    |
| Pretax earnings:   |                                      |        |                                 |         |
| Aflac Japan  | \$839                                | \$757  | \$1,677                         | \$1,576 |
| Aflac U.S.   | 291                                  | 293    | 623                             | 578     |
| Other business segments                                      | 5                                    | 3      | 8                               | 4       |
| Total business segment pretax operating earnings             | 1,135                                | 1,053  | 2,308                           | 2,158   |
| Interest expense, noninsurance operations                    | (30 )                                | (38 )  | (59 )                           | (87 )   |
| Corporate and eliminations                                   | (26 )                                | (20 )  | (61 )                           | (41 )   |
| Pretax operating earnings                                    | 1,079                                | 995    | 2,188                           | 2,030   |
| Realized investment gains (losses) <sup>(1)</sup>            | (208 )                               | 104    | (157 )                          | 100     |
| Other non-operating income (loss)                            | (37 )                                | (225 ) | (80 )                           | (243 )  |
| Total earnings before income taxes                           | \$834                                | \$874  | \$1,951                         | \$1,887 |
| Income taxes applicable to pretax operating earnings         | \$372                                | \$344  | \$755                           | \$701   |
| Effect of foreign currency translation on operating earnings | 36                                   | (59 )  | 49                              | (117 )  |

<sup>(1)</sup> Excluding a gain of \$21 and \$23 for the three-month periods and \$43 and \$40 for the six-month periods ended June 30, 2016, and 2015, respectively, related to the interest rate component of the change in fair value of foreign currency swaps on notes payable which is classified as an operating gain when analyzing segment operations

Assets were as follows:

| (In millions)                 | June 30,<br>2016 | December 31,<br>2015 |
|-------------------------------|------------------|----------------------|
| Assets:                       |                  |                      |
| Aflac Japan                   | \$120,571        | \$97,646             |
| Aflac U.S.                    | 19,712           | 18,537               |
| Other business segments       | 248              | 188                  |
| Total business segment assets | 140,531          | 116,371              |
| Corporate                     | 28,189           | 23,375               |
| Intercompany eliminations     | (27,433 )        | (21,490 )            |
| Total assets                  | \$141,287        | \$118,256            |

Prior-year amounts have been adjusted for the adoption of accounting guidance on January 1, 2016 related to debt issuance costs.



## 3. INVESTMENTS

## Investment Holdings

The amortized cost for our investments in debt and perpetual securities, the cost for equity securities and the fair values of these investments are shown in the following tables.

| (In millions)   | June 30, 2016          |                        |                         | Fair Value |
|---|------------------------|------------------------|-------------------------|------------|
|   | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses |            |
| Securities available for sale, carried at fair value: |                        |                        |                         |            |
| Fixed maturities:                                     |                        |                        |                         |            |
| Yen-denominated:                                      |                        |                        |                         |            |
| Japan government and agencies                         | \$22,176               | \$ 5,828               | \$ 0                    | \$28,004   |
| Municipalities  | 200                    | 60                     | 0                       | 260        |
| Mortgage- and asset-backed securities                 | 870                    | 51                     | 0                       | 921        |
| Public utilities                                      | 1,639                  | 277                    | 13                      | 1,903      |
| Sovereign and supranational                           | 927                    | 189                    | 0                       | 1,116      |
| Banks/financial institutions                          | 2,704                  | 382                    | 119                     | 2,967      |
| Other corporate                                       | 3,926                  | 650                    | 55                      | 4,521      |
| Total yen-denominated                                 | 32,442                 | 7,437                  | 187                     | 39,692     |
| Dollar-denominated:                                   |                        |                        |                         |            |
| U.S. government and agencies                          | 123                    | 16                     | 0                       | 139        |
| Municipalities  | 943                    | 164                    | 7                       | 1,100      |
| Mortgage- and asset-backed securities                 | 199                    | 18                     | 0                       | 217        |
| Public utilities                                      | 5,724                  | 776                    | 76                      | 6,424      |
| Sovereign and supranational                           | 352                    | 97                     | 0                       | 449        |
| Banks/financial institutions                          | 2,742                  | 533                    | 16                      | 3,259      |
| Other corporate                                       | 27,474                 | 2,316                  | 784                     | 29,006     |
| Total dollar-denominated                              | 37,557                 | 3,920                  | 883                     | 40,594     |
| Total fixed maturities                                | 69,999                 | 11,357                 | 1,070                   | 80,286     |
| Perpetual securities:                                 |                        |                        |                         |            |
| Yen-denominated:                                      |                        |                        |                         |            |
| Banks/financial institutions                          | 1,650                  | 77                     | 199                     | 1,528      |
| Other corporate                                       | 214                    | 20                     | 0                       | 234        |
| Dollar-denominated:                                   |                        |                        |                         |            |
| Banks/financial institutions                          | 52                     | 18                     | 0                       | 70         |
| Total perpetual securities                            | 1,916                  | 115                    | 199                     | 1,832      |
| Equity securities:                                    |                        |                        |                         |            |
| Yen-denominated                                       | 694                    | 29                     | 76                      | 647        |
| Dollar-denominated                                    | 551                    | 17                     | 18                      | 550        |
| Total equity securities                               | 1,245                  | 46                     | 94                      | 1,197      |
| Total securities available for sale                   | \$73,160               | \$ 11,518              | \$ 1,363                | \$83,315   |

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| (In millions)   | June 30, 2016          |                        |                         | Fair Value |
|---|------------------------|------------------------|-------------------------|------------|
|   | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses |            |
| Securities held to maturity, carried at amortized cost: |                        |                        |                         |            |
| Fixed maturities:                                       |                        |                        |                         |            |
| Yen-denominated:  |                        |                        |                         |            |
| Japan government and agencies                           | \$23,440               | \$ 8,636               | \$ 0                    | \$32,076   |
| Municipalities  | 398                    | 167                    | 0                       | 565        |
| Mortgage- and asset-backed securities                   | 39                     | 2                      | 0                       | 41         |
| Public utilities  | 3,623                  | 415                    | 10                      | 4,028      |
| Sovereign and supranational                             | 2,994                  | 404                    | 7                       | 3,391      |
| Banks/financial institutions                            | 4,659                  | 293                    | 32                      | 4,920      |
| Other corporate   | 3,193                  | 590                    | 8                       | 3,775      |
| Total yen-denominated                                   | 38,346                 | 10,507                 | 57                      | 48,796     |
| Total securities held to maturity                       | \$38,346               | \$ 10,507              | \$ 57                   | \$48,796   |



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| (In millions)   | December 31, 2015      |                        |                         | Fair Value |
|---|------------------------|------------------------|-------------------------|------------|
|   | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses |            |
| Securities available for sale, carried at fair value: |                        |                        |                         |            |
| Fixed maturities:                                     |                        |                        |                         |            |
| Yen-denominated:                                      |                        |                        |                         |            |
| Japan government and agencies                         | \$17,293               | \$ 1,862               | \$ 0                    | \$19,155   |
| Municipalities  | 128                    | 9                      | 0                       | 137        |
| Mortgage- and asset-backed securities                 | 322                    | 33                     | 0                       | 355        |
| Public utilities                                      | 1,400                  | 210                    | 10                      | 1,600      |
| Sovereign and supranational                           | 791                    | 180                    | 0                       | 971        |
| Banks/financial institutions                          | 2,321                  | 325                    | 105                     | 2,541      |
| Other corporate                                       | 3,337                  | 448                    | 33                      | 3,752      |
| Total yen-denominated                                 | 25,592                 | 3,067                  | 148                     | 28,511     |
| Dollar-denominated:                                   |                        |                        |                         |            |
| U.S. government and agencies                          | 110                    | 11                     | 0                       | 121        |
| Municipalities  | 926                    | 151                    | 6                       | 1,071      |
| Mortgage- and asset-backed securities                 | 200                    | 27                     | 0                       | 227        |
| Public utilities                                      | 5,464                  | 636                    | 221                     | 5,879      |
| Sovereign and supranational                           | 331                    | 105                    | 0                       | 436        |
| Banks/financial institutions                          | 2,865                  | 634                    | 21                      | 3,478      |
| Other corporate                                       | 25,154                 | 1,774                  | 1,302                   | 25,626     |
| Total dollar-denominated                              | 35,050                 | 3,338                  | 1,550                   | 36,838     |
| Total fixed maturities                                | 60,642                 | 6,405                  | 1,698                   | 65,349     |
| Perpetual securities:                                 |                        |                        |                         |            |
| Yen-denominated:                                      |                        |                        |                         |            |
| Banks/financial institutions                          | 1,581                  | 143                    | 93                      | 1,631      |
| Other corporate                                       | 183                    | 22                     | 0                       | 205        |
| Dollar-denominated:                                   |                        |                        |                         |            |
| Banks/financial institutions                          | 77                     | 35                     | 1                       | 111        |
| Total perpetual securities                            | 1,841                  | 200                    | 94                      | 1,947      |
| Equity securities:                                    |                        |                        |                         |            |
| Yen-denominated                                       | 472                    | 19                     | 4                       | 487        |
| Dollar-denominated                                    | 8                      | 3                      | 0                       | 11         |
| Total equity securities                               | 480                    | 22                     | 4                       | 498        |
| Total securities available for sale                   | \$62,963               | \$ 6,627               | \$ 1,796                | \$67,794   |

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| (In millions)   | December 31, 2015      |                        |                         | Fair Value |
|---|------------------------|------------------------|-------------------------|------------|
|   | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses |            |
| Securities held to maturity, carried at amortized cost: |                        |                        |                         |            |
| Fixed maturities:                                       |                        |                        |                         |            |
| Yen-denominated:  |                        |                        |                         |            |
| Japan government and agencies                           | \$20,004               | \$ 3,387               | \$ 0                    | \$23,391   |
| Municipalities  | 341                    | 74                     | 0                       | 415        |
| Mortgage- and asset-backed securities                   | 36                     | 2                      | 0                       | 38         |
| Public utilities  | 3,092                  | 205                    | 94                      | 3,203      |
| Sovereign and supranational                             | 2,555                  | 182                    | 26                      | 2,711      |
| Banks/financial institutions                            | 4,431                  | 168                    | 53                      | 4,546      |
| Other corporate   | 3,000                  | 260                    | 44                      | 3,216      |
| Total yen-denominated                                   | 33,459                 | 4,278                  | 217                     | 37,520     |
| Total securities held to maturity                       | \$33,459               | \$ 4,278               | \$ 217                  | \$37,520   |

The methods of determining the fair values of our investments in fixed-maturity securities, perpetual securities and equity securities are described in Note 5.

Beginning in 2015 and continuing into the first six months of 2016, we increased our investment in yen-denominated publicly traded equity securities. During the first six months of 2016, we also increased our investment in U.S. dollar-denominated publicly traded equity securities. These securities are classified as available for sale and carried on our balance sheet at fair value.

During the first and second quarters of 2016 and 2015, respectively, we did not reclassify any investments from the held-to-maturity category to the available-for-sale category.

#### Contractual and Economic Maturities

The contractual maturities of our investments in fixed maturities at June 30, 2016, were as follows:

| (In millions)                             | Aflac Japan    |            | Aflac U.S.     |            |
|---|----------------|------------|----------------|------------|
|   | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Available for sale:                       |                |            |                |            |
| Due in one year or less                   | \$305          | \$312      | \$60           | \$62       |
| Due after one year through five years     | 3,882          | 3,972      | 722            | 789        |
| Due after five years through 10 years     | 11,905         | 12,101     | 2,487          | 2,726      |
| Due after 10 years                        | 40,332         | 48,573     | 8,776          | 10,124     |
| Mortgage- and asset-backed securities     | 926            | 988        | 34             | 41         |
| Total fixed maturities available for sale | \$57,350       | \$65,946   | \$12,079       | \$13,742   |
| Held to maturity:                         |                |            |                |            |
| Due in one year or less                   | \$49           | \$49       | \$0            | \$0        |
| Due after one year through five years     | 1,983          | 2,087      | 0              | 0          |
| Due after five years through 10 years     | 2,084          | 2,283      | 0              | 0          |
| Due after 10 years                        | 34,191         | 44,336     | 0              | 0          |
| Mortgage- and asset-backed securities     | 39             | 41         | 0              | 0          |
| Total fixed maturities held to maturity   | \$38,346       | \$48,796   | \$0            | \$0        |

At June 30, 2016, the Parent Company and other business segments had portfolios of available-for-sale fixed-maturity securities totaling \$570 million at amortized cost and \$598 million at fair value, which are not included in the table above.



Expected maturities may differ from contractual maturities because some issuers have the right to call or prepay obligations with or without call or prepayment penalties.

The majority of our perpetual securities are subordinated to other debt obligations of the issuer, but rank higher than the issuer's equity securities. Perpetual securities have characteristics of both debt and equity investments, along with unique features that create economic maturity dates for the securities. Although perpetual securities have no contractual maturity date, they have stated interest coupons that were fixed at their issuance and subsequently change to a floating short-term interest rate after some period of time. The instruments are generally callable by the issuer at the time of changing from a fixed coupon rate to a new variable rate of interest, which is determined by the combination of some market index plus a fixed amount of basis points. The net effect is to create an expected maturity date for the instrument. The economic maturities of our investments in perpetual securities, which were all reported as available for sale at June 30, 2016, were as follows:

| (In millions)                                 | Aflac Japan    |            | Aflac U.S.     |            |
|---|----------------|------------|----------------|------------|
|   | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Due in one year or less                       | \$221          | \$195      | \$0            | \$0        |
| Due after one year through five years         | 306            | 316        | 0              | 0          |
| Due after 10 years                            | 1,350          | 1,269      | 39             | 52         |
| Total perpetual securities available for sale | \$1,877        | \$1,780    | \$39           | \$52       |

#### Investment Concentrations

Our process for credit-related investments begins with an independent approach to underwriting each issuer's fundamental credit quality. We evaluate independently those factors which we believe could influence an issuer's ability to make payments under the contractual terms of our instruments. This includes a thorough analysis of a variety of items including the issuer's country of domicile (including political, legal, and financial considerations); the industry in which the issuer competes (with an analysis of industry structure, end-market dynamics, and regulation); company specific issues (such as management, assets, earnings, cash generation, and capital needs); and contractual provisions of the instrument (such as financial covenants and position in the capital structure). We further evaluate the investment considering broad business and portfolio management objectives, including asset/liability needs, portfolio diversification, and expected income.

Investment exposures that individually exceeded 10% of shareholders' equity as of June 30, 2016 and December 31, 2015 were as follows:

| (In millions)                            | June 30, 2016 |                |            | December 31, 2015 |                |            |
|--|---------------|----------------|------------|-------------------|----------------|------------|
|  | Credit Rating | Amortized Cost | Fair Value | Credit Rating     | Amortized Cost | Fair Value |
| Japan National Government <sup>(1)</sup> | A             | \$45,064       | \$59,305   | A                 | \$36,859       | \$42,025   |

<sup>(1)</sup>Japan Government Bonds (JGBs) or JGB-backed securities

## Realized Investment Gains and Losses

Information regarding pretax realized gains and losses from investments is as follows:

| (In millions)                            | Three<br>Months<br>Ended<br>June 30,<br>2016 |       | Six Months<br>Ended<br>June 30,<br>2015 |       |
|--|--|-------|---|-------|
| Realized investment gains (losses):      |  |       |   |       |
| Fixed maturities:                        |  |       |   |       |
| Available for sale:                      |  |       |   |       |
| Gross gains from sales                   | \$6  | \$55  | \$8                                     | \$104 |
| Gross losses from sales                  | (12 )  | 0     | (16 )                                   | 0     |
| Net gains (losses) from redemptions      | (5 )   | 7     | 78                                      | 26    |
| Other-than-temporary impairment losses   | (9 )   | 0     | (21 )                                   | (6 )  |
| Total fixed maturities                   | (20 )  | 62    | 49                                      | 124   |
| Perpetual securities:                    |  |       |   |       |
| Available for sale:                      |  |       |   |       |
| Net gains (losses) from redemptions      | 30   | 30    | 40                                      | 30    |
| Other-than-temporary impairment losses   | 0  | 0     | (2 )                                    | 0     |
| Total perpetual securities               | 30   | 30    | 38                                      | 30    |
| Equity securities:                       |  |       |   |       |
| Gross gains from sales                   | 2  | 0     | 5                                       | 0     |
| Gross losses from sales                  | (8 )   | 0     | (11 )                                   | 0     |
| Other-than-temporary impairment losses   | (24 )  | 0     | (24 )                                   | 0     |
| Total equity securities                  | (30 )  | 0     | (30 )                                   | 0     |
| Derivatives and other:                   |  |       |   |       |
| Derivative gains (losses)                | (167 )                                       | 35    | (171 )                                  | (14 ) |
| Total derivatives and other              | (167 )                                       | 35    | (171 )                                  | (14 ) |
| Total realized investment gains (losses) | \$(187)                                      | \$127 | \$(114)                                 | \$140 |

## Other-than-temporary Impairment

The majority of our fixed maturity and perpetual security investments are evaluated for other-than-temporary impairment using our debt impairment model. Our debt impairment model focuses on the ultimate collection of the cash flows from our investments and whether we have the intent to sell or if it is more likely than not we would be required to sell the security prior to recovery of its amortized cost. The fair values of our fixed maturity and perpetual security investments fluctuate based on changes in interest rates, foreign exchange, and credit spreads in the global financial markets. Fair values can also be heavily influenced by the values of the assets of the issuer and expected ultimate recovery values upon a default, bankruptcy or other financial restructuring. Credit spreads are most impacted by the general credit environment and global market liquidity. Interest rates are driven by numerous factors including, but not limited to, supply and demand, governmental monetary actions, expectations of inflation and economic growth. We believe that fluctuations in the fair values of our investment securities related to general changes in the level of credit spreads or interest rates have little bearing on underlying credit quality of the issuer, and whether our investment is ultimately recoverable. Generally, we consider such declines in fair values to be temporary even in situations where an investment remains in an unrealized loss position for an extended period of time.

In the course of our review process, we may determine that it is unlikely that our fixed maturity or perpetual security investment will recover in value within an acceptable time frame. Factors which may influence this determination include the severity of the price decline, the length of time the price has been impaired, if the price decline was driven

by issuer credit deterioration, and our view of the likelihood of the security defaulting or otherwise being subject to an unfavorable restructuring. In those cases where we believe the security will not recover in price within an acceptable period of time, we consider such a decline in the investment's fair value, to the extent it is below the investment's cost or amortized cost, to be an other-than-temporary impairment of the investment and reduce the book value of the investment to its fair value.

The perpetual securities we hold were largely issued by banks that are integral to the financial markets of the sovereign country of the issuer. As a result of the issuer's position within the economy of the sovereign country, our perpetual securities may be subject to a higher risk of nationalization of their issuers in connection with capital injections from an issuer's sovereign government. We cannot be assured that such capital support will extend to all levels of an issuer's capital structure. In addition, certain governments or regulators may consider imposing interest and principal payment restrictions on issuers of hybrid securities to preserve cash and preserve the issuer's capital. Beyond the cash flow impact that additional deferrals would have on our portfolio, such deferrals could result in ratings downgrades of the affected securities, which in turn could result in a reduction of fair value of the securities and increase our regulatory capital requirements. We consider these factors in our credit review process.

When determining our intention to sell a security prior to recovery of its fair value to amortized cost, we evaluate facts and circumstances such as, but not limited to, future cash flow needs, decisions to reposition our security portfolio, and risk profile of individual investment holdings. We perform ongoing analyses of our liquidity needs, which includes cash flow testing of our policy liabilities, debt maturities, projected dividend payments and other cash flow and liquidity needs. Our cash flow testing includes extensive duration analysis of our investment portfolio and policy liabilities. Based on our analyses, we have concluded that we have sufficient excess cash flows to meet our liquidity needs without selling any of our investments prior to their maturity.

Our investments in perpetual securities that are rated below investment grade and equity securities are evaluated for other-than-temporary impairment under our equity impairment model. Our equity impairment model focuses on the severity of a security's decline in fair value coupled with the length of time the fair value of the security has been below cost or amortized cost and the financial condition and near-term prospects of the issuer. For equity securities, we also verify our intent to hold the securities until they recover in value. The fair value of our investments in equity securities may decline for various reasons, such as general market conditions which reflect prospects for the economy as a whole, or due to specific information pertaining to an industry or an individual company. For those equity securities evaluated for impairment under the equity impairment model that are in an unrealized loss position, if we believe the security will not recover in price within an acceptable period of time, or we do not have the intent to hold until recovery, we will record an other-than-temporary impairment of the investment and reduce the cost of the investment to its fair value on that date.

The following table details our pretax other-than-temporary impairment losses by investment category that resulted from our impairment evaluation process.

|  | Three<br>Months<br>Ended<br>June 30,<br>2016 |      | Six<br>Months<br>Ended<br>June 30,<br>2015 |      |
|--|--|------|--|------|
| (In millions)  | 2016   | 2015 | 2016                                       | 2015 |
| Perpetual securities   | \$0  | \$ 0 | \$2  | \$ 0 |
| Corporate bonds  | 9  | 0    | 21   | 2    |
| Bank/financial institution bonds                                     | 0  | 0    | 0  | 4    |
| Equity securities  | 24   | 0    | 24   | 0    |
| Total other-than-temporary impairment losses realized <sup>(1)</sup> | \$33   | \$ 0 | \$47                                       | \$ 6 |

<sup>(1)</sup> Includes \$33 and an immaterial amount for the three-month periods and \$47 and \$6 for the six-month periods ended June 30, 2016 and 2015, respectively, from change in intent to sell securities or change in intent to hold securities until recovery

#### Unrealized Investment Gains and Losses

##### Effect on Shareholders' Equity

The net effect on shareholders' equity of unrealized gains and losses from investment securities was as follows:

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| (In millions)  | June 30,<br>2016 | December 31,<br>2015 |
|--|------------------|----------------------|
| Unrealized gains (losses) on securities available for sale               | \$10,155         | \$ 4,831             |
| Deferred income taxes  | (3,714 )         | (1,845 )             |
| Shareholders' equity, unrealized gains (losses) on investment securities | \$6,441          | \$ 2,986             |

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## Gross Unrealized Loss Aging

The following tables show the fair values and gross unrealized losses of our available-for-sale and held-to-maturity investments that were in an unrealized loss position, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

| (In millions)                 | June 30, 2016 |                   |                     |                   |                     |                   |
|-------------------------------|---------------|-------------------|---------------------|-------------------|---------------------|-------------------|
|                               | Total         |                   | Less than 12 months |                   | 12 months or longer |                   |
|                               | Fair Value    | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses |
| Fixed Maturities:             |               |                   |                     |                   |                     |                   |
| Municipalities:               |               |                   |                     |                   |                     |                   |
| Dollar-denominated            | \$46          | \$ 7              | \$ 0                | \$ 0              | \$ 46               | \$ 7              |
| Public utilities:             |               |                   |                     |                   |                     |                   |
| Dollar-denominated            | 1,216         | 76                | 283                 | 12                | 933                 | 64                |
| Yen-denominated               | 823           | 23                | 182                 | 13                | 641                 | 10                |
| Sovereign and supranational:  |               |                   |                     |                   |                     |                   |
| Yen-denominated               | 236           | 7                 | 0                   | 0                 | 236                 | 7                 |
| Banks/financial institutions: |               |                   |                     |                   |                     |                   |
| Dollar-denominated            | 148           | 16                | 78                  | 6                 | 70                  | 10                |
| Yen-denominated               | 1,428         | 151               | 240                 | 3                 | 1,188               | 148               |
| Other corporate:              |               |                   |                     |                   |                     |                   |
| Dollar-denominated            | 8,556         | 784               | 3,203               | 255               | 5,353               | 529               |
| Yen-denominated               | 970           | 63                | 327                 | 18                | 643                 | 45                |
| Total fixed maturities        | 13,423        | 1,127             | 4,313               | 307               | 9,110               | 820               |
| Perpetual securities:         |               |                   |                     |                   |                     |                   |
| Yen-denominated               | 989           | 199               | 500                 | 42                | 489                 | 157               |
| Total perpetual securities    | 989           | 199               | 500                 | 42                | 489                 | 157               |
| Equity securities:            |               |                   |                     |                   |                     |                   |
| Dollar-denominated            | 268           | 18                | 268                 | 18                | 0                   | 0                 |
| Yen-denominated               | 411           | 76                | 411                 | 76                | 0                   | 0                 |
| Total equity securities       | 679           | 94                | 679                 | 94                | 0                   | 0                 |
| Total                         | \$15,091      | \$ 1,420          | \$ 5,492            | \$ 443            | \$ 9,599            | \$ 977            |

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| (In millions)                 | December 31, 2015      |                      |                                      |                      |                                      |                      |
|-------------------------------|------------------------|----------------------|--------------------------------------|----------------------|--------------------------------------|----------------------|
|                               | Total<br>Fair<br>Value | Unrealized<br>Losses | Less than 12 months<br>Fair<br>Value | Unrealized<br>Losses | 12 months or longer<br>Fair<br>Value | Unrealized<br>Losses |
| Fixed Maturities:             |                        |                      |                                      |                      |                                      |                      |
| Municipalities:               |                        |                      |                                      |                      |                                      |                      |
| Dollar-denominated            | \$80                   | \$ 6                 | \$80                                 | \$ 6                 | \$0                                  | \$ 0                 |
| Public utilities:             |                        |                      |                                      |                      |                                      |                      |
| Dollar-denominated            | 2,127                  | 221                  | 1,689                                | 132                  | 438                                  | 89                   |
| Yen-denominated               | 1,487                  | 104                  | 1,062                                | 73                   | 425                                  | 31                   |
| Sovereign and supranational:  |                        |                      |                                      |                      |                                      |                      |
| Yen-denominated               | 580                    | 26                   | 385                                  | 13                   | 195                                  | 13                   |
| Banks/financial institutions: |                        |                      |                                      |                      |                                      |                      |
| Dollar-denominated            | 366                    | 21                   | 348                                  | 11                   | 18                                   | 10                   |
| Yen-denominated               | 2,350                  | 158                  | 1,147                                | 14                   | 1,203                                | 144                  |
| Other corporate:              |                        |                      |                                      |                      |                                      |                      |
| Dollar-denominated            | 13,430                 | 1,302                | 11,068                               | 770                  | 2,362                                | 532                  |
| Yen-denominated               | 1,151                  | 77                   | 343                                  | 5                    | 808                                  | 72                   |
| Total fixed maturities        | 21,571                 | 1,915                | 16,122                               | 1,024                | 5,449                                | 891                  |
| Perpetual securities:         |                        |                      |                                      |                      |                                      |                      |
| Dollar-denominated            | 6                      | 1                    | 0                                    | 0                    | 6                                    | 1                    |
| Yen-denominated               | 645                    | 93                   | 216                                  | 12                   | 429                                  | 81                   |
| Total perpetual securities    | 651                    | 94                   | 216                                  | 12                   | 435                                  | 82                   |
| Equity securities:            |                        |                      |                                      |                      |                                      |                      |
| Yen-denominated               | 191                    | 4                    | 191                                  | 4                    | 0                                    | 0                    |
| Total equity securities       | 191                    | 4                    | 191                                  | 4                    | 0                                    | 0                    |
| Total                         | \$22,413               | \$ 2,013             | \$16,529                             | \$ 1,040             | \$5,884                              | \$ 973               |

Analysis of Securities in Unrealized Loss Positions

The unrealized losses on our fixed maturity or perpetual securities investments have been primarily related to general market changes in interest rates, foreign exchange rates, and/or the levels of credit spreads rather than specific concerns with the issuer's ability to pay interest and repay principal. The unrealized losses on our investments in equity securities are primarily related to foreign exchange rates, general market conditions which reflect prospects for the economy as a whole, or specific information pertaining to an industry or an individual company.

For any significant declines in fair value of our fixed income or perpetual securities, we perform a more focused review of the related issuers' credit profile. For corporate issuers, we evaluate their assets, business profile including industry dynamics and competitive positioning, financial statements and other available financial data. For non-corporate issuers, we analyze all sources of credit support, including issuer-specific factors. We utilize information available in the public domain and, for certain private placement issuers, from consultations with the issuers directly. We also consider ratings from Nationally Recognized Statistical Rating Organizations (NRSROs), as well as the specific characteristics of the security we own including seniority in the issuer's capital structure, covenant predictions, or other relevant features. From these reviews, we evaluate the issuers' continued ability to service our investment through payment of interest and principal.

For any significant declines in fair value of our equity securities, we review the severity of the security's decline in fair value coupled with the length of time the fair value of the security has been below cost. We also perform a more focused review of the financial condition and near-term prospects of the issuer as well as general market conditions reflecting the prospects for the economy as a whole, and determine whether we have the intent to hold the securities

until they recover in value.

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The following table provides more information on our unrealized loss position on fixed maturities, perpetual securities and equity securities.

| (In millions)                   | June 30, 2016  |                               |  |   | December 31, 2015                                      |                               |  |   |     |   |     |   |
|---------------------------------|--|-------------------------------|--|---|--|-------------------------------|--|---|-----|---|-----|---|
|                                 | Investments<br>in an<br>Unrealized<br>Loss<br>Position | Gross<br>Unrealized<br>Losses | Gross<br>Unrealized<br>Losses that<br>are<br>Investment<br>Grade |   | Investments<br>in an<br>Unrealized<br>Loss<br>Position | Gross<br>Unrealized<br>Losses | Gross<br>Unrealized<br>Losses that<br>are<br>Investment<br>Grade |   |     |   |     |   |
| Fixed Maturities:               |  |                               |  |   |  |                               |  |   |     |   |     |   |
| Public utilities                | 13   | %                             | 7  | % | 88   | %                             | 16   | % | 16  | % | 93  | % |
| Sovereign and<br>supranational  | 2  |                               | 1  |   | 100  |                               | 3  |   | 1   |   | 100 |   |
| Banks/financial<br>institutions | 11   |                               | 12   |   | 36   |                               | 12   |   | 9   |   | 59  |   |
| Other corporate                 | 63   |                               | 59   |   | 47   |                               | 66   |   | 69  |   | 86  |   |
| Total fixed<br>maturities       | 89   |                               | 79   |   |  |                               | 97   |   | 95  |   |     |   |
| Perpetual securities            | 7  |                               | 14   |   | 100  |                               | 3  |   | 5   |   | 100 |   |
| Equity securities               | 4  |                               | 7  |   |  |                               | 0  |   | 0   |   |     |   |
| Total                           | 100  | %                             | 100  | % |  |                               | 100  | % | 100 | % |     |   |

The decrease in the percentage of gross unrealized losses that are investment grade for the banks and financial institutions sector for the period ending June 30, 2016 was due to the redemption of an investment-grade security that contributed to a large portion of investment-grade unrealized losses at December 31, 2015. The decrease in the percentage of gross unrealized loss for the other corporate sector for the period ending June 30, 2016 was due to the increase in unrealized losses of dollar-denominated below-investment-grade securities mainly attributable to the strengthening of the yen/dollar exchange rate.

Assuming no credit-related factors develop, unrealized gains and losses on fixed maturities and perpetual securities are expected to diminish as investments near maturity. Based on our credit analysis, we believe that the issuers of our fixed maturity and perpetual security investments in the sectors shown in the table above have the ability to service their obligations to us.

#### Variable Interest Entities (VIEs)

As a condition of our involvement or investment in a VIE, we enter into certain protective rights and covenants that preclude changes in the structure of the VIE that would alter the creditworthiness of our investment or our beneficial interest in the VIE.

For those VIEs in which we are not the arranger, our involvement is passive in nature. We are not, nor have we been, required to purchase any securities issued in the future by these VIEs.

Our ownership interest in VIEs is limited to holding the obligations issued by them. We have no direct or contingent obligations to fund the limited activities of these VIEs, nor do we have any direct or indirect financial guarantees related to the limited activities of these VIEs. We have not provided any assistance or any other type of financing support to any of the VIEs we invest in, nor do we have any intention to do so in the future. For those VIEs in which we hold debt obligations, the weighted-average lives of our notes are very similar to the underlying collateral held by these VIEs where applicable.

We also utilize unit trust structures in our Aflac Japan segment to invest in various asset classes. As the arranger and sole investor of these VIEs, we are required to consolidate these entities under U.S. GAAP.

Our risk of loss related to our interests in any of our VIEs is limited to the carrying value of the related investments held in the VIE.

## VIEs - Consolidated

The following table presents the cost or amortized cost, fair value and balance sheet caption in which the assets and liabilities of consolidated VIEs are reported.

## Investments in Consolidated Variable Interest Entities

| (In millions)                            | June 30, 2016          |            | December 31, 2015      |            |
|--|------------------------|------------|------------------------|------------|
|  | Cost or Amortized Cost | Fair Value | Cost or Amortized Cost | Fair Value |
| <b>Assets:</b>                           |                        |            |                        |            |
| Fixed maturities, available for sale     | \$4,878                | \$5,493    | \$3,739                | \$4,554    |
| Perpetual securities, available for sale | 267                    | 197        | 255                    | 228        |
| Equity securities                        | 1,018                  | 941        | 363                    | 363        |
| Other investments                        | 165                    | 169        | 0                      | 0          |
| Other assets                             | 177                    | 177        | 102                    | 102        |
| Total assets of consolidated VIEs        | \$6,505                | \$6,977    | \$4,459                | \$5,247    |
| <b>Liabilities:</b>                      |                        |            |                        |            |
| Other liabilities                        | \$117                  | \$117      | \$293                  | \$293      |
| Total liabilities of consolidated VIEs   | \$117                  | \$117      | \$293                  | \$293      |

We are substantively the only investor in the consolidated VIEs listed in the table above. As the sole investor in these VIEs, we have the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and are therefore considered to be the primary beneficiary of the VIEs that we consolidate. We also participate in substantially all of the variability created by these VIEs. The activities of these VIEs are limited to holding debt, equity, and perpetual securities and foreign currency, and/or credit default swaps (CDS), as appropriate, and utilizing the cash flows from these securities to service our investment. Neither we nor any of our creditors are able to obtain the underlying collateral of the VIEs unless there is an event of default or other specified event. For those VIEs that contain a swap, we are not a direct counterparty to the swap contracts and have no control over them. Our loss exposure to these VIEs is limited to our original investment. Our consolidated VIEs do not rely on outside or ongoing sources of funding to support their activities beyond the underlying collateral and swap contracts, if applicable. With the exception of our investment in senior secured bank loans (bank loans), commercial mortgage loans, and certain equity securities through unit trust structures, the underlying collateral assets and funding of our consolidated VIEs are generally static in nature and the underlying collateral and the reference corporate entities covered by any CDS contracts were all investment grade at the time of issuance.

We invest in bank loans, yen-denominated public equities, dollar-denominated public equities, and commercial mortgage loans through unit trust structures in which we are the only investor, requiring us to consolidate these trusts under U.S. GAAP. The bank loans are classified as available-for-sale fixed-maturity securities in the financial statements. As of June 30, 2016, the amortized cost and fair value of our bank loan investments was \$2.1 billion and \$1.9 billion, respectively, compared with an amortized cost and fair value of \$1.4 billion as of December 31, 2015. The yen-denominated and dollar-denominated equities are classified as available-for-sale in the financial statements. As of June 30, 2016, the amortized cost and fair value of these equities was \$1.0 billion and \$941 million, respectively, compared with amortized cost and fair value of \$363 million as of December 31, 2015. The commercial mortgage loans, all of which were purchased in the first six months of 2016, are classified as held for investment and reflected in other investments on the consolidated balance sheets. As of June 30, 2016, the amortized cost of these loans, net of loan loss reserves, was \$165 million.

We are exposed to credit losses within our consolidated collateralized debt obligation (CDO) that could result in principal losses to our investment. However, we have mitigated the risk of credit loss through the structure of the VIE,

which contractually requires the subordinated tranches within the VIE to absorb the majority of the expected losses from the underlying credit default swaps. We currently own only senior mezzanine CDO tranches. Based on our statistical analysis models and the current subordination levels in our CDO, the VIE can sustain a reasonable number of defaults in the underlying reference entities in the CDS with no loss to our investment.

## VIEs-Not Consolidated

The table below reflects the amortized cost, fair value and balance sheet caption in which our investment in VIEs not consolidated are reported.

## Investments in Variable Interest Entities Not Consolidated

| (In millions)                              | June 30, 2016  |            | December 31, 2015 |            |
|--|----------------|------------|-------------------|------------|
|  | Amortized Cost | Fair Value | Amortized Cost    | Fair Value |
| Assets:                                    |                |            |                   |            |
| Fixed maturities, available for sale       | \$5,158        | \$5,656    | \$4,731           | \$5,093    |
| Perpetual securities, available for sale   | 292            | 279        | 249               | 253        |
| Fixed maturities, held to maturity         | 2,902          | 3,336      | 2,477             | 2,636      |
| Total investments in VIEs not consolidated | \$8,352        | \$9,271    | \$7,457           | \$7,982    |

Prior-year amounts have been adjusted for the adoption of accounting guidance on January 1, 2016 related to consolidations.

The VIEs that we are not required to consolidate are investments that are in the form of debt obligations from the VIEs that are irrevocably and unconditionally guaranteed by their corporate parents or sponsors. These VIEs are the primary financing vehicles used by their corporate sponsors to raise financing in the capital markets. The variable interests created by these VIEs are principally or solely a result of the debt instruments issued by them. We do not have the power to direct the activities that most significantly impact the entity's economic performance, nor do we have the obligation to absorb losses of the entity or the right to receive benefits from the entity. As such, we are not the primary beneficiary of these VIEs and are therefore not required to consolidate them. These VIE investments comprise securities from 143 separate issuers with an average credit rating of BBB.

## Loans and Loan Receivables

We classify our loans and loan receivables as held-for-investment and include them in the other investments line on the consolidated balance sheets. We carry them on the balance sheet at amortized cost less an estimated allowance for loan losses. Our loan allowance for losses is established using both specific and general allowances. The specific allowance is used on an individual loan basis for those impaired loans where we expect to incur a loss. The general allowance is used for loans grouped by similar risk characteristics where a loan-specific or market-specific risk has not been identified, but for which we anticipate to incur a loss.

## Middle Market Loans

As of June 30, 2016, and December 31, 2015, our investment in middle market loan receivables, net of loan loss reserves, was \$227 million and \$118 million, respectively, which included an unfunded amount of \$31 million and \$53 million, respectively, that was reflected in other liabilities on the consolidated balance sheets. As of June 30, 2016 and December 31, 2015, we had no loans that were past due in regards to principal and/or interest payments. Additionally, we held no loans that were on nonaccrual status or considered impaired as of June 30, 2016 and December 31, 2015. Our middle market loan allowance for losses was immaterial as of June 30, 2016 and December 31, 2015. We had no troubled debt restructurings during the six months ended June 30, 2016 and 2015.

As of June 30, 2016, we had commitments of \$72 million to fund potential future loan originations related to this investment program. These commitments are contingent upon the availability of middle market loans that meet our underwriting criteria.

## Commercial Mortgage Loans



In 2016, we began funding investments in commercial mortgage loans. As of June 30, 2016, the amortized cost of these investments, net of loan loss reserves, was \$188 million, \$165 million of which was held in unit trust structures as discussed above. We had no loans that were past due in regards to principal and/or interest payments, and we held no loans that were on nonaccrual status or considered impaired as of June 30, 2016. Our commercial mortgage loan allowance for losses was immaterial as of June 30, 2016. We had no troubled debt restructurings during the six months ended June 30, 2016.

As of June 30, 2016, we had \$177 million in outstanding commitments to fund commercial mortgage loans. These commitments are contingent on the final underwriting and due diligence to be performed.

#### Securities Lending and Pledged Securities

We lend fixed-maturity securities to financial institutions in short-term security-lending transactions. These short-term security-lending arrangements increase investment income with minimal risk. Our security lending policy requires that the fair value of the securities and/or unrestricted cash received as collateral be 102% or more of the fair value of the loaned securities. These securities continue to be carried as investment assets on our balance sheet during the terms of the loans and are not reported as sales. We receive cash or other securities as collateral for such loans. For loans involving unrestricted cash or securities as collateral, the collateral is reported as an asset with a corresponding liability for the return of the collateral.

Details of our securities lending activities were as follows:

#### Securities Lending Transactions Accounted for as Secured Borrowings

June 30, 2016

##### Remaining Contractual Maturity of the Agreements

| (In millions)                    | Overnight<br>and<br>Continuous <sup>(1)</sup> | Up<br>to 30<br>days | Total |
|----------------------------------|---|---------------------|-------|
| Securities lending transactions: |   |                     |       |
| Japan government and agencies    | \$ 0  | \$372               | \$372 |
| Public utilities                 | 104   | 0                   | 104   |
| Banks/financial institutions     | 24  | 0                   | 24    |
| Other corporate                  | 326   | 0                   | 326   |
| Total borrowings                 | \$ 454  | \$372               | \$826 |

Gross amount of recognized liabilities for securities lending transactions \$826

Amounts related to agreements not included in offsetting disclosure in Note 4 \$0

<sup>(1)</sup> These securities are pledged as collateral under our U.S. securities lending program and can be called at our discretion; therefore, they are classified as Overnight and Continuous.

#### Securities Lending Transactions Accounted for as Secured Borrowings

December 31, 2015

##### Remaining Contractual Maturity of the Agreements

| (In millions)                    | Overnight<br>and<br>Continuous <sup>(1)</sup> | Up<br>to 30<br>days | Total |
|----------------------------------|---|---------------------|-------|
| Securities lending transactions: |   |                     |       |
| Japan government and agencies    | \$ 0  | \$499               | \$499 |
| Public utilities                 | 108   | 0                   | 108   |
| Banks/financial institutions     | 13  | 0                   | 13    |
| Other corporate                  | 321   | 0                   | 321   |
| Total borrowings                 | \$ 442  | \$499               | \$941 |

Gross amount of recognized liabilities for securities lending transactions \$941

\$0

Amounts related to agreements not included in  
offsetting disclosure in Note 4

<sup>(1)</sup> These securities are pledged as collateral under our U.S. securities lending program and can be called at our discretion; therefore, they are classified as Overnight and Continuous.

We did not have any repurchase agreements or repurchase-to-maturity transactions outstanding as of June 30, 2016 and December 31, 2015, respectively.

Certain fixed-maturity securities have been pledged as collateral as part of derivative transactions, or pledged to support state deposit requirements or certain investment programs. For additional information regarding pledged securities related to derivative transactions, see Note 4.

#### 4. DERIVATIVE INSTRUMENTS

Our freestanding derivative financial instruments consist of: (1) foreign currency swaps and credit default swaps that are associated with investments in special-purpose entities, including VIEs where we are the primary beneficiary; (2) foreign currency forwards and options used in hedging foreign exchange risk on U.S. dollar-denominated securities in Aflac Japan's portfolio; (3) foreign currency forwards and options used to hedge foreign exchange risk from our net investment in Aflac Japan and economically hedge certain portions of forecasted cash flows denominated in yen; (4) swaps associated with our notes payable, consisting of cross-currency interest rate swaps, also referred to as foreign currency swaps, associated with certain senior notes and our subordinated debentures; and (5) options on interest rate swaps (or interest rate swaptions) and futures used to hedge interest rate risk for certain available-for-sale securities. We do not use derivative financial instruments for trading purposes, nor do we engage in leveraged derivative transactions. Some of our derivatives are designated as cash flow hedges, fair value hedges or net investment hedges; however, other derivatives do not qualify for hedge accounting or we elect not to designate them as an accounting hedge. We utilize a net investment hedge to mitigate foreign exchange exposure resulting from our net investment in Aflac Japan. In addition to designating derivatives as hedging instruments, we have designated our yen-denominated Samurai and Uridashi notes as nonderivative hedging instruments for this net investment hedge.

##### Derivative Types

We enter into foreign currency swaps pursuant to which we exchange an initial principal amount in one currency for an initial principal amount of another currency, with an agreement to re-exchange the currencies at a future date at an agreed upon exchange rate. There may also be periodic exchanges of payments at specified intervals based on the agreed upon rates and notional amounts. Foreign currency swaps are used primarily in the consolidated VIEs in our Aflac Japan portfolio to convert foreign-denominated cash flows to yen, the functional currency of Aflac Japan, in order to minimize cash flow fluctuations. We also use foreign currency swaps to economically convert certain of our dollar-denominated senior note and subordinated debenture principal and interest obligations into yen-denominated obligations.

Foreign currency forwards and options are executed for the Aflac Japan segment in order to hedge the currency risk on the fair value of certain fixed-maturity U.S. dollar-denominated securities. The majority of these forwards and options have short-term maturities (12 months or less). In forward transactions, Aflac Japan agrees with another party to buy a fixed amount of yen and sell a corresponding amount of U.S. dollars at a specified future date. Aflac Japan also executes foreign currency option transactions in a collar strategy, where Aflac Japan agrees with another party to simultaneously purchase a fixed amount of U.S. dollar put options and sell U.S. dollar call options. The combination of these two actions results in no net premium being paid (i.e. a costless or zero-cost collar). The foreign currency forwards and options are used in fair value hedging relationships to mitigate the foreign exchange risk associated with dollar-denominated investments supporting yen-denominated liabilities.

Foreign currency forwards and options are also used to hedge the currency risk associated with the net investment in Aflac Japan. In these forward transactions, Aflac agrees with another party to buy a fixed amount of U.S. dollars and sell a corresponding amount of yen at a specified future date. In the option transactions, we use a combination of foreign currency options to protect expected future cash flows by simultaneously purchasing yen put options (options that protect against a weakening yen) and selling yen call options (options that limit participation in a strengthening yen). The combination of these two actions results in no net premium being paid (i.e. a costless or zero-cost collar).

The only CDS that we currently hold relates to components of an investment in a VIE and is used to assume credit risk related to an individual security. This CDS contract entitles the consolidated VIE to receive periodic fees in exchange for an obligation to compensate the derivative counterparties should the referenced security issuer experience a credit event, as defined in the contract.

Interest rate swaps involve the periodic exchange of cash flows with other parties, at specified intervals, calculated using agreed upon rates or other financial variables and notional principal amounts. Typically, at the time a swap is entered into, the cash flow streams exchanged by the counterparties are equal in value. No cash or principal payments are exchanged at the inception of the contract. Interest rate swaps are primarily used to convert interest receipts on floating-rate fixed-maturity securities contracts to fixed rates. These derivatives are predominantly used to better match cash receipts from assets with cash disbursements required to fund liabilities.

Interest rate swaptions are options on interest rate swaps. Interest rate collars are combinations of two swaption positions and are executed in order to hedge certain U.S. dollar-denominated available-for-sale securities that are held in the Aflac Japan segment. We use collars to protect against significant changes in the fair value associated with our U.S. dollar-denominated available-for-sale securities due to interest rates. In order to maximize the efficiency of the collars while minimizing cost, we set the strike price on each collar so that the premium paid for the 'payer leg' is offset by the premium received for having sold the 'receiver leg'.

Periodically, depending on general economic conditions, we may enter into other derivative transactions.

#### Credit Risk Assumed through Derivatives

For the foreign currency and credit default swaps associated with our VIE investments for which we are the primary beneficiary, we bear the risk of foreign exchange loss due to counterparty default even though we are not a direct counterparty to those contracts. We are a direct counterparty to the foreign currency swaps that we have entered into in connection with certain of our senior notes, subordinated debentures, and Samurai notes; foreign currency forwards; foreign currency options; and interest rate swaptions, and therefore we are exposed to credit risk in the event of nonperformance by the counterparties in those contracts. The risk of counterparty default for our VIE swaps, foreign currency swaps, certain foreign currency forwards, foreign currency options and interest rate swaptions is mitigated by collateral posting requirements that counterparties to those transactions must meet. As of June 30, 2016, there were 15 counterparties to our derivative agreements, with five comprising 62% of the aggregate notional amount. The counterparties to these derivatives are financial institutions with the following credit ratings:

| (In millions)                  | June 30, 2016                  |                              |                                  | December 31, 2015              |                              |                                  |
|--------------------------------|--------------------------------|------------------------------|----------------------------------|--------------------------------|------------------------------|----------------------------------|
|                                | Notional Amount of Derivatives | Asset Derivatives Fair Value | Liability Derivatives Fair Value | Notional Amount of Derivatives | Asset Derivatives Fair Value | Liability Derivatives Fair Value |
| Counterparties' credit rating: |                                |                              |                                  |                                |                              |                                  |
| AA                             | \$2,875                        | \$ 173                       | \$ (126 )                        | \$2,187                        | \$ 166                       | \$ (35 )                         |
| A                              | 19,131                         | 1,691                        | (352 )                           | 19,940                         | 510                          | (336 )                           |
| BBB                            | 1,100                          | 99                           | (64 )                            | 0                              | 0                            | 0                                |
| Total                          | \$23,106                       | \$ 1,963                     | \$ (542 )                        | \$22,127                       | \$ 676                       | \$ (371 )                        |

We engage in derivative transactions directly with unaffiliated third parties under International Swaps and Derivatives Association, Inc. (ISDA) agreements and other documentation. Most of the ISDA agreements also include Credit Support Annex (CSA) provisions, which generally provide for two-way collateral postings, in certain cases at the first dollar of exposure and in other cases once various rating and exposure threshold levels are triggered. We mitigate the risk that counterparties to transactions might be unable to fulfill their contractual obligations by monitoring counterparty credit exposure and collateral value while generally requiring that collateral be posted at the outset of the transaction or that additional collateral be posted upon the occurrence of certain events or circumstances. In addition, a significant portion of the derivative transactions have provisions that require collateral to be posted upon a downgrade of our long-term debt ratings or give the counterparty the right to terminate the transaction upon a downgrade of Aflac's financial strength rating. The actual amount of collateral required to be posted to counterparties in the event of such downgrades, or the aggregate amount of payments that we could be required to make, depends on market conditions, the fair value of outstanding affected transactions, and other factors prevailing at and after the time of the downgrade.

The fair value of the collateral posted by us to third parties for derivative transactions was \$259 million at June 30, 2016, which consisted entirely of cash, compared with \$20 million at December 31, 2015, which consisted of \$17 million of pledged securities and \$3 million of cash. This collateral can generally be replugged or resold by the

counterparties. The aggregate fair value of all derivative instruments with credit-risk-related contingent features that were in a net liability position by counterparty was approximately \$248 million and \$26 million as of June 30, 2016 and December 31, 2015, respectively. If the credit-risk-related contingent features underlying these agreements had been triggered on June 30, 2016, we estimate that we would not be required to post any additional collateral to these derivative counterparties. Collateral obtained by us from third parties for derivative transactions was \$1.7 billion and \$412 million at June 30, 2016 and December 31, 2015, respectively. We are generally allowed to sell or repledge collateral obtained from our derivative counterparties, although we do not typically exercise such rights.

### Accounting for Derivative Financial Instruments

Freestanding derivatives are carried at estimated fair value in our consolidated balance sheets either as other assets or as other liabilities. See Note 5 for a discussion on how we determine the fair value of our derivatives. Accruals on derivatives are recorded in accrued investment income or within other liabilities in the consolidated balance sheets. If a derivative is not designated as an accounting hedge or its use in managing risk does not qualify for hedge accounting, changes in the estimated fair value of the derivative are generally reported within derivative and other gains(losses), which is a component of realized investment gains (losses). The fluctuations in estimated fair value of derivatives that have not been designated for hedge accounting can result in volatility in net earnings.

### Hedge Documentation and Effectiveness Testing

To qualify for hedge accounting treatment, a derivative must be highly effective in mitigating the designated risk of the hedged item. At the inception of the hedging relationship for hedges we elect to designate for hedge accounting treatment, we formally document all relationships between hedging instruments and hedged items, as well as our risk-management objective and strategy for undertaking each hedge transaction. We document the designation of each hedge as either (i) a hedge of the variability of cash flows to be received or paid related to a recognized asset or liability or the hedge of a forecasted transaction ("cash flow hedge"); (ii) a hedge of the estimated fair value of a recognized asset or liability ("fair value hedge"); or (iii) a hedge of a net investment in a foreign operation. The documentation process includes linking derivatives and nonderivatives that are designated as hedges to specific assets or groups of assets or liabilities on the statement of financial position or to specific forecasted transactions and defining the effectiveness and ineffectiveness testing methods to be used. At the hedge's inception and on an ongoing quarterly basis, we also formally assess whether the derivatives that are used in hedging transactions have been, and are expected to continue to be, highly effective in offsetting their designated risk. Hedge effectiveness is assessed using qualitative and quantitative methods.

For assessing hedge effectiveness of cash flow hedges, qualitative methods may include the comparison of critical terms of the derivative to the hedged item, and quantitative methods may include regression or other statistical analysis of changes in cash flows associated with the hedge relationship. Hedge ineffectiveness of the hedge relationships on our VIE cash flow hedges is measured each reporting period using the "Hypothetical Derivative Method." For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income (loss) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing hedge ineffectiveness are recognized in current earnings within derivative and other gains (losses). All components of each derivative's gain or loss are included in the assessment of hedge effectiveness.

For assessing hedge effectiveness of fair value hedges, qualitative methods may include the comparison of critical terms of the derivative to the hedged item, and quantitative methods may include regression or other statistical analysis of changes in fair value associated with the hedge relationship. Hedge ineffectiveness of the hedge relationships is measured each reporting period using the dollar offset method. For derivative instruments that are designated and qualify as fair value hedges, changes in the estimated fair value of the derivative, including amounts measured as ineffectiveness, and changes in the estimated fair value of the hedged item related to the designated risk being hedged, are reported in current earnings within derivative and other gains (losses). When assessing the effectiveness of our fair value hedges, we exclude the changes in fair value related to the difference between the spot and the forward rate on our foreign currency forwards and the time value of options.

For the hedge of our net investment in Aflac Japan, we have designated Parent Company yen-denominated liabilities as non-derivative hedging instruments and have designated certain foreign currency forwards and options as derivative hedging instruments. We make our net investment hedge designation at the beginning of each quarter. For assessing hedge effectiveness of net investment hedges, if the total of the designated Parent Company non-derivative and derivatives notional is equal to or less than our net investment in Aflac Japan, the hedge is deemed to be effective. If the hedge is effective, the related exchange effect on the yen-denominated liabilities is reported in the unrealized foreign currency component of other comprehensive income. For derivatives designated as net investment hedges, Aflac follows the forward-rate method. According to that method, all changes in fair value, including changes related to the forward-rate component of foreign currency forward contracts and the time value of foreign currency options, are reported in the unrealized foreign currency component of other comprehensive income. Should these designated



net investment hedge positions exceed our net investment in Aflac Japan, the foreign exchange effect on the portion that exceeds our investment in Aflac Japan would be recognized in current earnings within derivative and other gains (losses).

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### Discontinuance of Hedge Accounting

We discontinue hedge accounting prospectively when (1) it is determined that the derivative is no longer highly effective in offsetting changes in the estimated cash flows or fair value of a hedged item; (2) the derivative is de-designated as a hedging instrument; or (3) the derivative expires or is sold, terminated or exercised.

When hedge accounting is discontinued on a cash flow hedge or fair value hedge, the derivative is carried in the consolidated balance sheets at its estimated fair value, with changes in estimated fair value recognized in current period earnings. For discontinued cash flow hedges, including those where the derivative is sold, terminated or exercised, amounts previously deferred in other comprehensive income (loss) are reclassified into earnings when earnings are impacted by the cash flow of the hedged item.

### Derivative Balance Sheet Classification

The tables below summarize the balance sheet classification of our derivative fair value amounts, as well as the gross asset and liability fair value amounts. The fair value amounts presented do not include income accruals. The notional amount of derivative contracts represents the basis upon which pay or receive amounts are calculated. Notional amounts are not reflective of credit risk.

| (In millions)                      | June 30, 2016   |                   |                       |            |
|------------------------------------|-----------------|-------------------|-----------------------|------------|
|                                    | Net Derivatives | Asset Derivatives | Liability Derivatives |            |
| Hedge Designation/ Derivative Type | Notional Amount | Fair Value        | Fair Value            | Fair Value |
| Cash flow hedges:                  |                 |                   |                       |            |
| Foreign currency swaps             | \$75            | \$(1 )            | \$ 1                  | \$(2 )     |
| Total cash flow hedges             | 75              | (1 )              | 1                     | (2 )       |
| Fair value hedges:                 |                 |                   |                       |            |
| Foreign currency forwards          | 12,917          | 1,442             | 1,442                 | 0          |
| Foreign currency options           | 1,685           | 6                 | 7                     | (1 )       |
| Total fair value hedges            | 14,602          | 1,448             | 1,449                 | (1 )       |
| Net investment hedge:              |                 |                   |                       |            |
| Foreign currency forwards          | 846             | (93 )             | 0                     | (93 )      |
| Foreign currency options           | 710             | (48 )             | 4                     | (52 )      |
| Total net investment hedge         | 1,556           | (141 )            | 4                     | (145 )     |
| Non-qualifying strategies:         |                 |                   |                       |            |
| Foreign currency swaps             | 6,669           | 97                | 491                   | (394 )     |
| Foreign currency forwards          | 107             | 17                | 17                    | 0          |
| Credit default swaps               | 97              | 1                 | 1                     | 0          |
| Total non-qualifying strategies    | 6,873           | 115               | 509                   | (394 )     |
| Total derivatives                  | \$23,106        | \$ 1,421          | \$ 1,963              | \$(542 )   |
| Balance Sheet Location             |                 |                   |                       |            |
| Other assets                       | \$18,388        | \$ 1,963          | \$ 1,963              | \$ 0       |
| Other liabilities                  | 4,718           | (542 )            | 0                     | (542 )     |
| Total derivatives                  | \$23,106        | \$ 1,421          | \$ 1,963              | \$(542 )   |

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| (In millions)                      | December 31, 2015 |            |                   |                       |
|------------------------------------|-------------------|------------|-------------------|-----------------------|
|                                    | Net Derivatives   |            | Asset Derivatives | Liability Derivatives |
| Hedge Designation/ Derivative Type | Notional Amount   | Fair Value | Fair Value        | Fair Value            |
| <b>Cash flow hedges:</b>           |                   |            |                   |                       |
| Foreign currency swaps             | \$75              | \$ (15 )   | \$ 0              | \$ (15 )              |
| Total cash flow hedges             | 75                | (15 )      | 0                 | (15 )                 |
| <b>Fair value hedges:</b>          |                   |            |                   |                       |
| Foreign currency forwards          | 13,080            | 45         | 88                | (43 )                 |
| Foreign currency options           | 1,250             | 0          | 0                 | 0                     |
| Total fair value hedges            | 14,330            | 45         | 88                | (43 )                 |
| <b>Net investment hedge:</b>       |                   |            |                   |                       |
| Foreign currency forwards          | 763               | 13         | 19                | (6 )                  |
| Foreign currency options           | 266               | (3 )       | 5                 | (8 )                  |
| Total net investment hedge         | 1,029             | 10         | 24                | (14 )                 |
| <b>Non-qualifying strategies:</b>  |                   |            |                   |                       |
| Foreign currency swaps             | 6,599             | 264        | 563               | (299 )                |
| Foreign currency forwards          | 11                | 0          | 0                 | 0                     |
| Credit default swaps               | 83                | 1          | 1                 | 0                     |
| Total non-qualifying strategies    | 6,693             | 265        | 564               | (299 )                |
| Total derivatives                  | \$22,127          | \$ 305     | \$ 676            | \$ (371 )             |
| <b>Balance Sheet Location</b>      |                   |            |                   |                       |
| Other assets                       | \$11,413          | \$ 676     | \$ 676            | \$ 0                  |
| Other liabilities                  | 10,714            | (371 )     | 0                 | (371 )                |
| Total derivatives                  | \$22,127          | \$ 305     | \$ 676            | \$ (371 )             |

#### Cash Flow Hedges

Certain of our consolidated VIEs have foreign currency swaps that qualify for hedge accounting treatment. For those that have qualified, we have designated the derivative as a hedge of the variability in cash flows of a forecasted transaction or of amounts to be received or paid related to a recognized asset ("cash flow" hedge). We expect to continue this hedging activity for a weighted-average period of approximately 10 years. The remaining derivatives in our consolidated VIEs that have not qualified for hedge accounting have been designated as held for other investment purposes ("non-qualifying strategies").

#### Fair Value Hedges

We designate and account for certain foreign currency forwards and options as fair value hedges when they meet the requirements for hedge accounting. These foreign currency forwards and options hedge the foreign currency exposure of certain U.S. dollar-denominated fixed maturity securities within the investment portfolio of our Aflac Japan segment. We recognize gains and losses on these derivatives and the related hedged items in current earnings within derivative and other gains (losses). The change in the fair value of the foreign currency forwards related to the changes in the difference between the spot rate and the forward price is excluded from the assessment of hedge effectiveness. The change in fair value of the foreign currency option related to the time value of the option is excluded from the assessment of hedge effectiveness.

We designate and account for interest rate swaptions as fair value hedges when they meet the requirements for hedge accounting. These interest rate swaptions hedge the interest rate exposure of certain U.S. dollar-denominated fixed maturity securities within the investment portfolio of our Aflac Japan segment. We recognize gains and losses on these derivatives and the related hedged items in current earnings within derivative and other gains (losses). The change in the fair value of the interest rate swaptions related to the time value of the option is excluded from the assessment of hedge effectiveness.



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The following table presents the gains and losses on derivatives and the related hedged items in fair value hedges. Fair Value Hedging Relationships

| (In millions)                     |                           | Hedging Derivatives  |  |  | Hedged Items   |   |
|-----------------------------------|---------------------------|----------------------|--|--|----------------|---|
| Hedging Derivatives               | Hedged Items              | Total Gains (Losses) | Gains (Losses) Excluded from Effectiveness Testing | Gains (Losses) Included in Effectiveness Testing | Gains (Losses) | Ineffectiveness Recognized for Fair Value Hedge |
| Three Months Ended June 30, 2016: |                           |                      |  |  |                |   |
| Foreign currency forwards         | Fixed-maturity securities | \$1,156              | \$ (48 )   | \$ 1,204   | \$(1,236)      | \$ (32 )  |
| Foreign currency options          | Fixed-maturity securities | 7                    | 7  | 0  | 0              | 0   |
| Six Months Ended June 30, 2016:   |                           |                      |  |  |                |   |
| Foreign currency forwards         | Fixed-maturity securities | \$2,013              | \$ (92 )   | \$ 2,105   | \$(2,118)      | \$ (13 )  |
| Foreign currency options          | Fixed-maturity securities | 6                    | 6  | 0  | 0              | 0   |
| Three Months Ended June 30, 2015: |                           |                      |  |  |                |   |
| Foreign currency forwards         | Fixed-maturity securities | \$(267 )             | \$ (17 )   | \$ (250 )  | \$244          | \$ (6 )   |
| Foreign currency options          | Fixed-maturity securities | (5 )                 | 1  | (6 )   | 6              | 0   |
| Interest rate swaptions           | Fixed-maturity securities | (4 )                 | 0  | (4 )   | 5              | 1   |
| Six Months Ended June 30, 2015:   |                           |                      |  |  |                |   |
| Foreign currency forwards         | Fixed-maturity securities | \$(230 )             | \$ (32 )   | \$ (198 )  | \$205          | \$ 7  |
| Foreign currency options          | Fixed-maturity securities | (3 )                 | 4  | (7 )   | 7              | 0   |
| Interest rate swaptions           | Fixed-maturity securities | (95 )                | 19   | (114 )   | 99             | (15 )   |

Subsequent to the end of the second quarter, in July 2016 we began using foreign exchange forwards to hedge the currency risk of our senior secured bank loan portfolio and U.S. dollar-denominated equity portfolio within the Aflac Japan segment. The derivative notional amounts associated with the hedges of our senior secured bank loan portfolio and our U.S. equity portfolio is approximately \$1.9 billion and \$457 million, respectively.

#### Net Investment Hedge

Our primary exposure to be hedged is our net investment in Aflac Japan, which is affected by changes in the yen/dollar exchange rate. To mitigate this exposure, we have designated the Parent Company's yen-denominated liabilities (Samurai and Uridashi notes - see Note 7) as non-derivative hedges and designated foreign currency forwards and options as derivative hedges of the foreign currency exposure of our net investment in Aflac Japan.

We used foreign exchange forwards and options to hedge foreign exchange risk on 25.0 billion yen of profit repatriation received from Aflac Japan in February 2016. As of June 30, 2016, we had entered into foreign exchange forwards and options as part of a hedge on 51.1 billion yen of profit repatriation received in July 2016 and 109.0 billion yen of future profit repatriation.

Our net investment hedge was effective during the three- and six-month periods ended June 30, 2016 and 2015, respectively.



### Non-qualifying Strategies

For our derivative instruments in consolidated VIEs that do not qualify for hedge accounting treatment, all changes in their fair value are reported in current period earnings within derivative and other gains (losses). The amount of gain or loss recognized in earnings for our VIEs is attributable to the derivatives in those investment structures. While the change in value of the swaps is recorded through current period earnings, the change in value of the available-for-sale fixed-maturity or perpetual securities associated with these swaps is recorded through other comprehensive income. We have cross-currency interest rate swap agreements related to our \$400 million senior notes due February 2017, \$550 million senior notes due March 2020, \$350 million senior notes due February 2022, \$700 million senior notes due June 2023, \$750 million senior notes due November 2024, \$450 million senior notes due March 2025, and \$500 million subordinated debentures due September 2052. Changes in the values of these swaps are recorded through current period earnings.

For additional information regarding these swaps, see Note 7 in this report and Note 9 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015.

## Impact of Derivatives and Hedging Instruments

The following table summarizes the impact to realized investment gains (losses) and other comprehensive income (loss) from all derivatives and hedging instruments.

| (In millions)                            | Three Months Ended June 30,        |  |                                    |  | Six Months Ended June 30,          |  |                                    |  |
|--|------------------------------------|--|------------------------------------|--|------------------------------------|--|------------------------------------|--|
|  | 2016                               |  | 2015                               |  | 2016                               |  | 2015                               |  |
|  | Realized Investment Gains (Losses) | Other Comprehensive Income (Loss) <sup>(1)</sup> | Realized Investment Gains (Losses) | Other Comprehensive Income (Loss) <sup>(1)</sup> | Realized Investment Gains (Losses) | Other Comprehensive Income (Loss) <sup>(1)</sup> | Realized Investment Gains (Losses) | Other Comprehensive Income (Loss) <sup>(1)</sup> |
| Qualifying hedges:                       |                                    |  |                                    |  |                                    |  |                                    |  |
| Cash flow hedges:                        |                                    |  |                                    |  |                                    |  |                                    |  |
| Foreign currency swaps                   | \$1                                | \$ 8   | \$0                                | \$ 2   | \$1                                | \$ 11  | \$0                                | \$ (2 )  |
| Total cash flow hedges                   | 1                                  | 8  | 0                                  | 2  | 1                                  | 11   | 0                                  | (2 )   |
| Fair value hedges:                       |                                    |  |                                    |  |                                    |  |                                    |  |
| Foreign currency forwards <sup>(2)</sup> | (80 )                              | 0  | (23 )                              | 0  | (105 )                             | 0  | (25 )                              | 0  |
| Foreign currency options <sup>(2)</sup>  | 7                                  | 0  | 1                                  | 0  | 6                                  | 0  | 4                                  | 0  |
| Interest rate swaptions <sup>(2)</sup>   | 0                                  | 0  | 1                                  | 0  | 0                                  | 0  | 4                                  | 0  |
| Total fair value hedges                  | (73 )                              | 0  | (21 )                              | 0  | (99 )                              | 0  | (17 )                              | 0  |
| Net investment hedge:                    |                                    |  |                                    |  |                                    |  |                                    |  |
| Non-derivative hedging instruments       | 0                                  | (22 )  | 0                                  | 6  | 0                                  | (37 )  | 0                                  | 5  |
| Foreign currency forwards                | 0                                  | (83 )  | 0                                  | 32   | 0                                  | (133 )   | 0                                  | 34   |
| Foreign currency options                 | 0                                  | (15 )  | 0                                  | 0  | 0                                  | (31 )  | 0                                  | 0  |
| Total net investment hedge               | 0                                  | (120 )   | 0                                  | 38   | 0                                  | (201 )   | 0                                  | 39   |
| Non-qualifying strategies:               |                                    |  |                                    |  |                                    |  |                                    |  |
| Foreign currency                         | (104 )                             | 0  | 55                                 | 0  | (94 )                              | 0  | (2 )                               | 0  |



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|               |         |           |      |       |         |           |        |       |  |
|---------------|---------|-----------|------|-------|---------|-----------|--------|-------|--|
| swaps         |         |           |      |       |         |           |        |       |  |
| Foreign       |         |           |      |       |         |           |        |       |  |
| currency      | 10      | 0         | (1 ) | 0     | 21      | 0         | (1 )   | 0     |  |
| forwards      |         |           |      |       |         |           |        |       |  |
| Credit        |         |           |      |       |         |           |        |       |  |
| default       | (1 )    | 0         | 0    | 0     | 0       | 0         | 1      | 0     |  |
| swaps         |         |           |      |       |         |           |        |       |  |
| Interest rate |         |           |      |       |         |           |        |       |  |
| swaps         | 0       | 0         | 2    | 0     | 0       | 0         | 5      | 0     |  |
| Total non-    |         |           |      |       |         |           |        |       |  |
| qualifying    | (95 )   | 0         | 56   | 0     | (73 )   | 0         | 3      | 0     |  |
| strategies    |         |           |      |       |         |           |        |       |  |
| Total         | \$(167) | \$ (112 ) | \$35 | \$ 40 | \$(171) | \$ (190 ) | \$(14) | \$ 37 |  |

(1) Cash flow hedge items are recorded as unrealized gains (losses) on derivatives and net investment hedge items are recorded in the unrealized foreign currency translation gains (losses) line in the consolidated statement of comprehensive income (loss).

(2) Impact shown net of effect of hedged items (see Fair Value Hedges section of this Note 4 for further detail)

We reclassified a \$1 million gain related to our designated cash flow hedges from accumulated other comprehensive income (loss) into earnings for the three- and six-month periods ended June 30, 2016, and reclassified an immaterial amount for the three- and six-month periods ended June 30, 2015, respectively. There was no gain or loss reclassified from accumulated other comprehensive income (loss) into earnings related to the net investment hedge for the three- and six-month periods ended June 30, 2016 and 2015, respectively. As of June 30, 2016, deferred gains and losses on derivative instruments recorded in accumulated other comprehensive income that are expected to be reclassified to earnings during the next twelve months were immaterial.

#### Offsetting of Financial Instruments and Derivatives

Some of the Company's derivative instruments are subject to enforceable master netting arrangements that provide for the net settlement of all derivative contracts between the Parent Company or Aflac and its respective counterparty in the event of default or upon the occurrence of certain termination events. Collateral support agreements with certain of the master netting arrangements provide that the Company will receive or pledge financial collateral in the event either minimum thresholds, or in certain cases ratings levels, have been reached.

We have securities lending agreements with unaffiliated financial institutions that post collateral to us in return for the use of our fixed maturity securities (see Note 3). When we have entered into securities lending agreements with the same counterparty, the agreements generally provide for net settlement in the event of default by the counterparty. This right of set-off allows us to keep and apply collateral received if the counterparty failed to return the securities borrowed from us as contractually agreed.

The tables below summarize our derivatives and securities lending transactions, and as reflected in the tables, in accordance with U.S. GAAP, our policy is to not offset these financial instruments in the Consolidated Balance Sheets.

## Offsetting of Financial Assets and Derivative Assets

June 30, 2016

| (In millions)  | Gross Amount of Recognized Assets | Gross Amount Offset in Balance Sheet | Net Amount of Assets Presented in Balance Sheet | Gross Amounts Not Offset in Balance Sheet |                         | Net Amount |
|--|-----------------------------------|--------------------------------------|---|---|-------------------------|------------|
|  |                                   |                                      |   | Carrying Value of Financial Instruments   | Collateral Received     |            |
| Derivative assets:   |                                   |                                      |   |   |                         |            |
| Foreign currency swaps   | \$492                             | \$ 0                                 | \$ 492  | \$0                                       | \$(187 )                | \$ 305     |
| Foreign currency forwards  | 1,459                             | 0                                    | 1,459   | 0   | (1,554 )                | (95 )      |
| Foreign currency options   | 11                                | 0                                    | 11  | 0   | (6 )                    | 5          |
| Credit default swaps   | 1                                 | 0                                    | 1   | 0   | 0                       | 1          |
| Total derivative assets, subject to a master netting arrangement or offsetting arrangement | 1,963                             | 0                                    | 1,963   | 0   | (1,747 ) <sup>(1)</sup> | 216        |
| Securities lending and similar arrangements  | 801                               | 0                                    | 801   | 0   | (801 )                  | 0          |
| Total  | \$2,764                           | \$ 0                                 | \$ 2,764  | \$0                                       | \$(2,548)               | \$ 216     |

<sup>(1)</sup> Consists of \$1,509 of pledged securities and \$238 of cash.

December 31, 2015

| (In millions)  | Gross Amount of Recognized Assets | Gross Amount Offset in Balance Sheet | Net Amount of Assets Presented in Balance Sheet | Gross Amounts Not Offset in Balance Sheet |                       | Net Amount |
|--|-----------------------------------|--------------------------------------|---|---|-----------------------|------------|
|  |                                   |                                      |   | Carrying Value of Financial Instruments   | Collateral Received   |            |
| Derivative assets:   |                                   |                                      |   |   |                       |            |
| Foreign currency swaps   | \$563                             | \$ 0                                 | \$ 563  | \$0                                       | \$(313 )              | \$ 250     |
| Foreign currency forwards  | 107                               | 0                                    | 107   | 0   | (96 )                 | 11         |
| Foreign currency options   | 5                                 | 0                                    | 5   | 0   | (3 )                  | 2          |
| Credit default swaps   | 1                                 | 0                                    | 1   | 0   | 0                     | 1          |
| Total derivative assets, subject to a master netting arrangement | 676                               | 0                                    | 676   | 0   | (412 ) <sup>(1)</sup> | 264        |

or offsetting  
arrangement

|  |         |      |          |     |           |        |
|--|---------|------|----------|-----|-----------|--------|
| Securities lending and<br>similar arrangements | 921     | 0    | 921      | 0   | (921 )    | 0      |
| Total  | \$1,597 | \$ 0 | \$ 1,597 | \$0 | \$(1,333) | \$ 264 |

<sup>(1)</sup> Consists of \$86 of pledged securities and \$326 of cash.

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Offsetting of Financial Liabilities and Derivative Liabilities  
June 30, 2016

| (In millions)   | Gross Amount of Recognized Liabilities | Gross Amount Offset in Balance Sheet | Net Amount of Liabilities Presented in Balance Sheet | Gross Amounts Not Offset in Balance Sheet |                    |            |
|---|--|--------------------------------------|--|---|--------------------|------------|
|   |  |                                      |  | Carrying Value of Financial Instruments   | Collateral Pledged | Net Amount |
| Derivative liabilities:   |  |                                      |  |   |                    |            |
| Foreign currency swaps  | \$ (396 )                              | \$ 0                                 | \$ (396 )  | \$0                                       | \$ 111             | \$(285)    |
| Foreign currency forwards   | (93 )                                  | 0                                    | (93 )  | 0   | 95                 | 2          |
| Foreign currency options  | (53 )                                  | 0                                    | (53 )  | 0   | 53                 | 0          |
| Total derivative liabilities, subject to a master netting arrangement or offsetting arrangement | (542 )                                 | 0                                    | (542 )   | 0   | 259 <sup>(1)</sup> | (283 )     |
| Securities lending and similar arrangements   | (826 )                                 | 0                                    | (826 )   | 801                                       | 0                  | (25 )      |
| Total   | \$ (1,368 )                            | \$ 0                                 | \$ (1,368)   | \$801                                     | \$ 259             | \$(308)    |

<sup>(1)</sup> Consists entirely of cash.  
December 31, 2015

| (In millions)   | Gross Amount of Recognized Liabilities | Gross Amount Offset in Balance Sheet | Net Amount of Liabilities Presented in Balance Sheet | Gross Amounts Not Offset in Balance Sheet |                    |            |
|---|--|--------------------------------------|--|---|--------------------|------------|
|   |  |                                      |  | Carrying Value of Financial Instruments   | Collateral Pledged | Net Amount |
| Derivative liabilities:   |  |                                      |  |   |                    |            |
| Foreign currency swaps  | \$ (314 )                              | \$ 0                                 | \$ (314 )  | \$0                                       | \$ 1               | \$(313)    |
| Foreign currency forwards   | (49 )                                  | 0                                    | (49 )  | 0   | 18                 | (31 )      |
| Foreign currency options  | (8 )                                   | 0                                    | (8 )   | 0   | 1                  | (7 )       |
| Total derivative liabilities, subject to a master netting arrangement or offsetting arrangement | (371 )                                 | 0                                    | (371 )   | 0   | 20 <sup>(1)</sup>  | (351 )     |
| Securities lending and similar arrangements   | (941 )                                 | 0                                    | (941 )   | 921                                       | 0                  | (20 )      |
| Total   | \$ (1,312)                             | \$ 0                                 | \$ (1,312)   | \$921                                     | \$ 20              | \$(371)    |

<sup>(1)</sup> Consists of \$17 of pledged securities and \$3 of cash.

For additional information on our financial instruments, see the accompanying Notes 1, 3 and 5 and Notes 1, 3 and 5 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended

December 31, 2015.

## 5. FAIR VALUE MEASUREMENTS

### Fair Value Hierarchy

U.S. GAAP specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. These two types of inputs create three valuation hierarchy levels. Level 1 valuations reflect quoted market prices for identical assets or liabilities in active markets. Level 2 valuations reflect quoted market prices for similar assets or liabilities in an active market, quoted market prices for identical or similar assets or liabilities in non-active markets or model-derived valuations in which all significant valuation inputs are observable in active markets. Level 3 valuations reflect valuations in which one or more of the significant inputs are not observable in an active market.

The following tables present the fair value hierarchy levels of the Company's assets and liabilities that are measured and carried at fair value on a recurring basis.

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| (In millions)  | June 30, 2016   |  |  |                        |
|--|---|--|--|------------------------|
|  | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
| Assets:  |   |  |  |                        |
| Securities available for sale, carried at<br>fair value: |   |  |  |                        |
| Fixed maturities:  |   |  |  |                        |
| Government and agencies                                  | \$27,284  | \$ 859   | \$ 0   | \$28,143               |
| Municipalities   | 0   | 1,360  | 0  | 1,360                  |
| Mortgage- and asset-backed securities                    | 0   | 886  | 252  | 1,138                  |
| Public utilities   | 0   | 8,327  | 0  | 8,327                  |
| Sovereign and supranational                              | 0   | 1,565  | 0  | 1,565                  |
| Banks/financial institutions                             | 0   | 6,200  | 26   | 6,226                  |
| Other corporate  | 0   | 33,527   | 0  | 33,527                 |
| Total fixed maturities                                   | 27,284  | 52,724   | 278  | 80,286                 |
| Perpetual securities:                                    |   |  |  |                        |
| Banks/financial institutions                             | 0   | 1,598  | 0  | 1,598                  |
| Other corporate  | 0   | 234  | 0  | 234                    |
| Total perpetual securities                               | 0   | 1,832  | 0  | 1,832                  |
| Equity securities  | 1,188   | 6  | 3  | 1,197                  |
| Other assets:  |   |  |  |                        |
| Foreign currency swaps                                   | 0   | 316  | 176  | 492                    |
| Foreign currency forwards                                | 0   | 1,459  | 0  | 1,459                  |
| Foreign currency options                                 | 0   | 11   | 0  | 11                     |
| Credit default swaps                                     | 0   | 0  | 1  | 1                      |
| Total other assets                                       | 0   | 1,786  | 177  | 1,963                  |
| Other investments  | 207   | 0  | 0  | 207                    |
| Cash and cash equivalents                                | 3,700   | 0  | 0  | 3,700                  |
| Total assets   | \$32,379  | \$ 56,348  | \$ 458   | \$89,185               |
| Liabilities:   |   |  |  |                        |
| Foreign currency swaps                                   | \$0   | \$ 279   | \$ 117   | \$396                  |
| Foreign currency forwards                                | 0   | 93   | 0  | 93                     |
| Foreign currency options                                 | 0   | 53   | 0  | 53                     |
| Total liabilities  | \$0   | \$425  | \$ 117   | \$542                  |

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| (In millions)   | December 31, 2015   |  |  |                        |
|---|---|--|--|------------------------|
|   | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
| Assets:   |   |  |  |                        |
| Securities available for sale, carried at fair value: |   |  |  |                        |
| Fixed maturities:                                     |   |  |  |                        |
| Government and agencies                               | \$18,669  | \$ 607   | \$ 0   | \$19,276               |
| Municipalities  | 0   | 1,208  | 0  | 1,208                  |
| Mortgage- and asset-backed securities                 | 0   | 362  | 220  | 582                    |
| Public utilities                                      | 0   | 7,479  | 0  | 7,479                  |
| Sovereign and supranational                           | 0   | 1,407  | 0  | 1,407                  |
| Banks/financial institutions                          | 0   | 5,993  | 26   | 6,019                  |
| Other corporate                                       | 0   | 29,378   | 0  | 29,378                 |
| Total fixed maturities                                | 18,669  | 46,434   | 246  | 65,349                 |
| Perpetual securities:                                 |   |  |  |                        |
| Banks/financial institutions                          | 0   | 1,742  | 0  | 1,742                  |
| Other corporate                                       | 0   | 205  | 0  | 205                    |
| Total perpetual securities                            | 0   | 1,947  | 0  | 1,947                  |
| Equity securities                                     | 489   | 6  | 3  | 498                    |
| Other assets:   |   |  |  |                        |
| Foreign currency swaps                                | 0   | 462  | 101  | 563                    |
| Foreign currency forwards                             | 0   | 107  | 0  | 107                    |
| Foreign currency options                              | 0   | 5  | 0  | 5                      |
| Credit default swaps                                  | 0   | 0  | 1  | 1                      |
| Total other assets                                    | 0   | 574  | 102  | 676                    |
| Other investments                                     | 176   | 0  | 0  | 176                    |
| Cash and cash equivalents                             | 4,350   | 0  | 0  | 4,350                  |
| Total assets  | \$23,684  | \$48,961   | \$ 351   | \$72,996               |
| Liabilities:  |   |  |  |                        |
| Foreign currency swaps                                | \$0   | \$21   | \$ 293   | \$314                  |
| Foreign currency forwards                             | 0   | 49   | 0  | 49                     |
| Foreign currency options                              | 0   | 8  | 0  | 8                      |
| Total liabilities                                     | \$0   | \$78   | \$ 293   | \$371                  |



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The following tables present the carrying amount and fair value categorized by fair value hierarchy level for the Company's financial instruments that are not carried at fair value.

| (In millions)   | June 30, 2016  |  |   |   |                  |
|---|----------------|--|---|---|------------------|
|   | Carrying Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value |
| Assets:   |                |  |   |   |                  |
| Securities held to maturity, carried at amortized cost: |                |  |   |   |                  |
| Fixed maturities:                                       |                |  |   |   |                  |
| Government and agencies                                 | \$23,440       | \$32,076   | \$0                                     | \$0                                       | \$32,076         |
| Municipalities  | 398            | 0  | 565                                     | 0   | 565              |
| Mortgage and asset-backed securities                    | 39             | 0  | 13                                      | 28  | 41               |
| Public utilities  | 3,623          | 0  | 4,028                                   | 0   | 4,028            |
| Sovereign and supranational                             | 2,994          | 0  | 3,391                                   | 0   | 3,391            |
| Banks/financial institutions                            | 4,659          | 0  | 4,920                                   | 0   | 4,920            |
| Other corporate   | 3,193          | 0  | 3,775                                   | 0   | 3,775            |
| Other investments                                       | 415            | 0  | 0                                       | 421                                       | 421              |
| Total assets  | \$38,761       | \$32,076   | \$16,692                                | \$449                                     | \$49,217         |
| Liabilities:  |                |  |   |   |                  |
| Other policyholders' funds                              | \$7,468        | \$0  | \$0                                     | \$7,327                                   | \$7,327          |
| Notes payable (excluding capital leases)                | 4,987          | 0  | 0                                       | 5,522                                     | 5,522            |
| Total liabilities                                       | \$12,455       | \$0  | \$0                                     | \$12,849                                  | \$12,849         |

| (In millions)   | December 31, 2015 |  |   |   |                  |
|---|-------------------|--|---|---|------------------|
|   | Carrying Value    | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value |
| Assets:   |                   |  |   |   |                  |
| Securities held to maturity, carried at amortized cost: |                   |  |   |   |                  |
| Fixed maturities:                                       |                   |  |   |   |                  |
| Government and agencies                                 | \$20,004          | \$23,391   | \$ 0                                    | \$ 0                                      | \$23,391         |
| Municipalities  | 341               | 0  | 415                                     | 0   | 415              |
| Mortgage and asset-backed securities                    | 36                | 0  | 12                                      | 26  | 38               |
| Public utilities  | 3,092             | 0  | 3,203                                   | 0   | 3,203            |
| Sovereign and supranational                             | 2,555             | 0  | 2,711                                   | 0   | 2,711            |
| Banks/financial institutions                            | 4,431             | 0  | 4,546                                   | 0   | 4,546            |
| Other corporate   | 3,000             | 0  | 3,216                                   | 0   | 3,216            |
| Other investments                                       | 118               | 0  | 0                                       | 118                                       | 118              |
| Total assets  | \$33,577          | \$23,391   | \$ 14,103                               | \$ 144                                    | \$37,638         |
| Liabilities:  |                   |  |   |   |                  |
| Other policyholders' funds                              | \$6,285           | \$0  | \$0                                     | \$ 6,160                                  | \$6,160          |
| Notes payable (excluding capital leases)                | 4,991             | 0  | 0                                       | 5,285                                     | 5,285            |
| Total liabilities                                       | \$11,276          | \$0  | \$0                                     | \$ 11,445                                 | \$11,445         |

#### Fair Value of Financial Instruments

U.S. GAAP requires disclosure of the fair value of certain financial instruments including those that are not carried at fair value. The carrying amounts for cash and cash equivalents, other investments (excluding loan receivables), receivables, accrued investment income, accounts payable, cash collateral and payables for security transactions approximated their fair values due to the nature of these instruments. Liabilities for future policy benefits and unpaid policy claims are not financial instruments as defined by U.S. GAAP.

#### Fixed maturities, perpetual securities, and equity securities

We determine the fair values of our fixed maturity securities, perpetual securities, and public and privately issued equity securities using the following approaches or techniques: price quotes and valuations from third party pricing vendors (including quoted market prices readily available from public exchange markets) and non-binding price quotes we obtain from outside brokers.

A third party pricing vendor has developed valuation models to determine fair values of privately issued securities to reflect the impact of the persistent economic environment and the changing regulatory framework. These models are discounted cash flow (DCF) valuation models, but also use information from related markets, specifically the CDS market to estimate expected cash flows. These models take into consideration any unique characteristics of the securities and make various adjustments to arrive at an appropriate issuer-specific loss adjusted credit curve. This

credit curve is then used with the relevant recovery rates to estimate expected cash flows and modeling of additional features, including illiquidity adjustments, if necessary, to price the security by discounting those loss adjusted cash flows. In cases where a credit curve cannot be developed from the specific security features, the valuation methodology takes into consideration other market observable inputs, including: 1) the most appropriate comparable security(ies) of the issuer; 2) issuer-specific CDS spreads; 3) bonds or CDS spreads of comparable issuers with similar characteristics such as rating, geography, or sector; or 4) bond indices that are comparative in rating, industry, maturity and region.

The pricing data and market quotes we obtain from outside sources, including third party pricing services, are reviewed internally for reasonableness. If a fair value appears unreasonable, we will re-examine the inputs and assess the reasonableness of the pricing data with the vendor. Additionally, we may compare the inputs to relevant market indices and other performance measurements. The output of this analysis is presented to the Company's Valuation and Classification Subcommittee (VCS). Based on the analysis provided to the VCS, the valuation is confirmed or may be revised if there is evidence of a more appropriate estimate of fair value based on available market data. We have performed verification of the inputs and calculations in any valuation models to confirm that the valuations represent reasonable estimates of fair value.

The fixed maturities classified as Level 3 consist of securities for which there are limited or no observable valuation inputs. For Level 3 securities that are investment grade, we estimate the fair value of these securities by obtaining non-binding broker quotes from a limited number of brokers. These brokers base their quotes on a combination of their knowledge of the current pricing environment and market conditions. We consider these inputs to be unobservable. For Level 3 investments that are below-investment-grade securities, we consider a variety of significant valuation inputs in the valuation process, including forward exchange rates, yen swap rates, dollar swap rates, interest rate volatilities, credit spread data on specific issuers, assumed default and default recovery rates, and certain probability assumptions. In obtaining these valuation inputs, we have determined that certain pricing assumptions and data used by our pricing sources are difficult to validate or corroborate by the market and/or appear to be internally developed rather than observed in or corroborated by the market. The use of these unobservable valuation inputs causes more subjectivity in the valuation process for these securities.

For the periods presented, we have not adjusted the quotes or prices we obtain from the pricing services and brokers we use.

The following tables present the pricing sources for the fair values of our fixed maturities, perpetual securities, and equity securities.



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| (In millions)   | June 30, 2016   |  |  | Total<br>Fair<br>Value |
|---|---|--|--|------------------------|
|   | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |                        |
| Securities available for sale, carried at fair value: |   |  |  |                        |
| Fixed maturities:                                     |   |  |  |                        |
| Government and agencies:                              |   |  |  |                        |
| Third party pricing vendor                            | \$27,284  | \$ 859   | \$ 0   | \$28,143               |
| Total government and agencies                         | 27,284  | 859  | 0  | 28,143                 |
| Municipalities:                                       |   |  |  |                        |
| Third party pricing vendor                            | 0   | 1,360  | 0  | 1,360                  |
| Total municipalities                                  | 0   | 1,360  | 0  | 1,360                  |
| Mortgage- and asset-backed securities:                |   |  |  |                        |
| Third party pricing vendor                            | 0   | 886  | 0  | 886                    |
| Broker/other  | 0   | 0  | 252  | 252                    |
| Total mortgage- and asset-backed securities           | 0   | 886  | 252  | 1,138                  |
| Public utilities:                                     |   |  |  |                        |
| Third party pricing vendor                            | 0   | 8,327  | 0  | 8,327                  |
| Total public utilities                                | 0   | 8,327  | 0  | 8,327                  |
| Sovereign and supranational:                          |   |  |  |                        |
| Third party pricing vendor                            | 0   | 1,565  | 0  | 1,565                  |
| Total sovereign and supranational                     | 0   | 1,565  | 0  | 1,565                  |
| Banks/financial institutions:                         |   |  |  |                        |
| Third party pricing vendor                            | 0   | 6,200  | 0  | 6,200                  |
| Broker/other  | 0   | 0  | 26   | 26                     |
| Total banks/financial institutions                    | 0   | 6,200  | 26   | 6,226                  |
| Other corporate:                                      |   |  |  |                        |
| Third party pricing vendor                            | 0   | 33,527   | 0  | 33,527                 |
| Total other corporate                                 | 0   | 33,527   | 0  | 33,527                 |
| Total fixed maturities                                | 27,284  | 52,724   | 278  | 80,286                 |
| Perpetual securities:                                 |   |  |  |                        |
| Banks/financial institutions:                         |   |  |  |                        |
| Third party pricing vendor                            | 0   | 1,598  | 0  | 1,598                  |
| Total banks/financial institutions                    | 0   | 1,598  | 0  | 1,598                  |
| Other corporate:                                      |   |  |  |                        |
| Third party pricing vendor                            | 0   | 234  | 0  | 234                    |
| Total other corporate                                 | 0   | 234  | 0  | 234                    |
| Total perpetual securities                            | 0   | 1,832  | 0  | 1,832                  |
| Equity securities:                                    |   |  |  |                        |
| Third party pricing vendor                            | 1,188   | 6  | 0  | 1,194                  |
| Broker/other  | 0   | 0  | 3  | 3                      |
| Total equity securities                               | 1,188   | 6  | 3  | 1,197                  |
| Total securities available for sale                   | \$28,472  | \$ 54,562  | \$ 281   | \$83,315               |



| (In millions)   | June 30, 2016   |  |  | Total<br>Fair<br>Value |
|---|---|--|--|------------------------|
|   | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |                        |
| Securities held to maturity, carried at amortized cost: |   |  |  |                        |
| Fixed maturities:                                       |   |  |  |                        |
| Government and agencies:                                |   |  |  |                        |
| Third party pricing vendor                              | \$32,076  | \$ 0   | \$ 0   | \$32,076               |
| Total government and agencies                           | 32,076  | 0  | 0  | 32,076                 |
| Municipalities:   |   |  |  |                        |
| Third party pricing vendor                              | 0   | 565  | 0  | 565                    |
| Total municipalities                                    | 0   | 565  | 0  | 565                    |
| Mortgage- and asset-backed securities:                  |   |  |  |                        |
| Third party pricing vendor                              | 0   | 13   | 0  | 13                     |
| Broker/other  | 0   | 0  | 28   | 28                     |
| Total mortgage- and asset-backed securities             | 0   | 13   | 28   | 41                     |
| Public utilities:                                       |   |  |  |                        |
| Third party pricing vendor                              | 0   | 4,028  | 0  | 4,028                  |
| Total public utilities                                  | 0   | 4,028  | 0  | 4,028                  |
| Sovereign and supranational:                            |   |  |  |                        |
| Third party pricing vendor                              | 0   | 3,391  | 0  | 3,391                  |
| Total sovereign and supranational                       | 0   | 3,391  | 0  | 3,391                  |
| Banks/financial institutions:                           |   |  |  |                        |
| Third party pricing vendor                              | 0   | 4,823  | 0  | 4,823                  |
| Broker/other  | 0   | 97   | 0  | 97                     |
| Total banks/financial institutions                      | 0   | 4,920  | 0  | 4,920                  |
| Other corporate:  |   |  |  |                        |
| Third party pricing vendor                              | 0   | 3,775  | 0  | 3,775                  |
| Total other corporate                                   | 0   | 3,775  | 0  | 3,775                  |
| Total securities held to maturity                       | \$32,076  | \$ 16,692  | \$ 28  | \$48,796               |



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| (In millions)   | December 31, 2015   |  |  | Total<br>Fair<br>Value |
|---|---|--|--|------------------------|
|   | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |                        |
| Securities available for sale, carried at fair value: |   |  |  |                        |
| Fixed maturities:                                     |   |  |  |                        |
| Government and agencies:                              |   |  |  |                        |
| Third party pricing vendor                            | \$ 18,669   | \$ 607   | \$ 0   | \$ 19,276              |
| Total government and agencies                         | 18,669  | 607  | 0  | 19,276                 |
| Municipalities:                                       |   |  |  |                        |
| Third party pricing vendor                            | 0   | 1,208  | 0  | 1,208                  |
| Total municipalities                                  | 0   | 1,208  | 0  | 1,208                  |
| Mortgage- and asset-backed securities:                |   |  |  |                        |
| Third party pricing vendor                            | 0   | 362  | 0  | 362                    |
| Broker/other  | 0   | 0  | 220  | 220                    |
| Total mortgage- and asset-backed securities           | 0   | 362  | 220  | 582                    |
| Public utilities:                                     |   |  |  |                        |
| Third party pricing vendor                            | 0   | 7,479  | 0  | 7,479                  |
| Total public utilities                                | 0   | 7,479  | 0  | 7,479                  |
| Sovereign and supranational:                          |   |  |  |                        |
| Third party pricing vendor                            | 0   | 1,407  | 0  | 1,407                  |
| Total sovereign and supranational                     | 0   | 1,407  | 0  | 1,407                  |
| Banks/financial institutions:                         |   |  |  |                        |
| Third party pricing vendor                            | 0   | 5,993  | 0  | 5,993                  |
| Broker/other  | 0   | 0  | 26   | 26                     |
| Total banks/financial institutions                    | 0   | 5,993  | 26   | 6,019                  |
| Other corporate:                                      |   |  |  |                        |
| Third party pricing vendor                            | 0   | 29,378   | 0  | 29,378                 |
| Total other corporate                                 | 0   | 29,378   | 0  | 29,378                 |
| Total fixed maturities                                | 18,669  | 46,434   | 246  | 65,349                 |
| Perpetual securities:                                 |   |  |  |                        |
| Banks/financial institutions:                         |   |  |  |                        |
| Third party pricing vendor                            | 0   | 1,742  | 0  | 1,742                  |
| Total banks/financial institutions                    | 0   | 1,742  | 0  | 1,742                  |
| Other corporate:                                      |   |  |  |                        |
| Third party pricing vendor                            | 0   | 205  | 0  | 205                    |
| Total other corporate                                 | 0   | 205  | 0  | 205                    |
| Total perpetual securities                            | 0   | 1,947  | 0  | 1,947                  |
| Equity securities:                                    |   |  |  |                        |
| Third party pricing vendor                            | 489   | 6  | 0  | 495                    |
| Broker/other  | 0   | 0  | 3  | 3                      |
| Total equity securities                               | 489   | 6  | 3  | 498                    |
| Total securities available for sale                   | \$ 19,158   | \$ 48,387  | \$ 249   | \$ 67,794              |



| (In millions)   | December 31, 2015   |  |  | Total<br>Fair<br>Value |
|---|---|--|--|------------------------|
|   | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |                        |
| Securities held to maturity, carried at amortized cost: |   |  |  |                        |
| Fixed maturities:                                       |   |  |  |                        |
| Government and agencies:                                |   |  |  |                        |
| Third party pricing vendor                              | \$23,391  | \$ 0   | \$ 0   | \$23,391               |
| Total government and agencies                           | 23,391  | 0  | 0  | 23,391                 |
| Municipalities:   |   |  |  |                        |
| Third party pricing vendor                              | 0   | 415  | 0  | 415                    |
| Total municipalities                                    | 0   | 415  | 0  | 415                    |
| Mortgage- and asset-backed securities:                  |   |  |  |                        |
| Third party pricing vendor                              | 0   | 12   | 0  | 12                     |
| Broker/other  | 0   | 0  | 26   | 26                     |
| Total mortgage- and asset-backed securities             | 0   | 12   | 26   | 38                     |
| Public utilities:                                       |   |  |  |                        |
| Third party pricing vendor                              | 0   | 3,203  | 0  | 3,203                  |
| Total public utilities                                  | 0   | 3,203  | 0  | 3,203                  |
| Sovereign and supranational:                            |   |  |  |                        |
| Third party pricing vendor                              | 0   | 2,711  | 0  | 2,711                  |
| Total sovereign and supranational                       | 0   | 2,711  | 0  | 2,711                  |
| Banks/financial institutions:                           |   |  |  |                        |
| Third party pricing vendor                              | 0   | 4,546  | 0  | 4,546                  |
| Total banks/financial institutions                      | 0   | 4,546  | 0  | 4,546                  |
| Other corporate:  |   |  |  |                        |
| Third party pricing vendor                              | 0   | 3,189  | 0  | 3,189                  |
| Broker/other  | 0   | 27   | 0  | 27                     |
| Total other corporate                                   | 0   | 3,216  | 0  | 3,216                  |
| Total securities held to maturity                       | \$23,391  | \$ 14,103  | \$ 26  | \$37,520               |

The following is a discussion of the determination of fair value of our remaining financial instruments.

#### Loan Receivables

Our loan receivables do not have readily determinable market prices and generally lack market liquidity. Fair values for loan receivables are determined based on the present value of expected future cash flows discounted at the applicable U.S. Treasury or LIBOR yield plus an appropriate spread that considers other risk factors, such as credit and liquidity risk. These spreads are provided by the applicable asset managers based on their knowledge of the current loan pricing environment and market conditions. The spreads are a significant component of the pricing inputs and are generally considered unobservable. Therefore, these investments have been assigned a Level 3 within the fair value hierarchy. Loan receivables are included in other investments on the consolidated balance sheets.

#### Derivatives

We use derivative instruments to manage the risk associated with certain assets. However, the derivative instrument may not be classified in the same fair value hierarchy level as the associated asset. Inputs used to value derivatives include, but are not limited to, interest rates, credit spreads, foreign currency forward and spot rates, and interest volatility.

The fair values of the foreign currency forwards, options, and interest rate swaptions associated with certain fixed-maturity securities; the foreign currency forwards and options used to hedge foreign exchange risk from our net investment in Aflac Japan and economically hedge certain portions of forecasted cash flows denominated in yen; and the foreign currency swaps associated with certain senior notes and our subordinated debentures are based on the amounts we would expect to receive or pay. The determination of the fair value of these derivatives is based on observable market inputs, therefore they are classified as Level 2.

For derivatives associated with VIEs where we are the primary beneficiary, we are not the direct counterparty to the swap contracts. As a result, the fair value measurements incorporate the credit risk of the collateral associated with the VIE. We receive valuations from a third party pricing vendor for these derivatives. Based on an analysis of these derivatives and a review of the methodology employed by the pricing vendor, we determined that due to the long duration of these swaps and the need to extrapolate from short-term observable data to derive and measure long-term inputs, certain inputs, assumptions and judgments are required to value future cash flows that cannot be corroborated by current inputs or current observable market data. As a result, the derivatives associated with our consolidated VIEs are classified as Level 3 of the fair value hierarchy.

#### Other policyholders' funds

The largest component of the other policyholders' funds liability is our annuity line of business in Aflac Japan. Our annuities have fixed benefits and premiums. For this product, we estimated the fair value to be equal to the cash surrender value. This is analogous to the value paid to policyholders on the valuation date if they were to surrender their policy. We periodically check the cash value against discounted cash flow projections for reasonableness. We consider our inputs for this valuation to be unobservable and have accordingly classified this valuation as Level 3.

#### Notes payable

The fair values of our publicly issued notes payable classified as Level 3 were obtained from a limited number of independent brokers. These brokers base their quotes on a combination of their knowledge of the current pricing environment and market conditions. We consider these inputs to be unobservable. The fair values of our yen-denominated loans approximate their carrying values.



## Transfers between Hierarchy Levels and Level 3 Rollforward

There were no transfers between Level 1 and 2 for the three- and six-month periods ended June 30, 2016 and 2015, respectively.

The following tables present the changes in fair value of our available-for-sale investments and derivatives classified as Level 3.

Three Months Ended  
June 30, 2016

| (In millions)  | Fixed Maturities                      |                               | Perpetual Securities          | Equity Securities | Derivatives <sup>(1)</sup> |                      | Total  |
|--|---------------------------------------|-------------------------------|-------------------------------|-------------------|----------------------------|----------------------|--------|
|  | Mortgage- and Asset-Backed Securities | Banks/ Financial Institutions | Banks/ Financial Institutions |                   | Foreign Currency Swaps     | Credit Default Swaps |        |
| Balance, beginning of period   | \$ 237                                | \$ 26                         | \$ 0                          | \$ 3              | \$ (63 )                   | \$ 2                 | \$ 205 |
| Realized investment gains (losses) included in earnings  | 0                                     | 0                             | 0                             | 0                 | 123                        | (1 )                 | 122    |
| Unrealized gains (losses) included in other comprehensive income (loss)  | 26                                    | 0                             | 0                             | 0                 | (1 )                       | 0                    | 25     |
| Purchases, issuances, sales and settlements:   |                                       |                               |                               |                   |                            |                      |        |
| Purchases  | 0                                     | 0                             | 0                             | 0                 | 0                          | 0                    | 0      |
| Issuances  | 0                                     | 0                             | 0                             | 0                 | 0                          | 0                    | 0      |
| Sales  | 0                                     | 0                             | 0                             | 0                 | 0                          | 0                    | 0      |
| Settlements  | (11 )                                 | 0                             | 0                             | 0                 | 0                          | 0                    | (11 )  |
| Transfers into Level 3   | 0                                     | 0                             | 0                             | 0                 | 0                          | 0                    | 0      |
| Transfers out of Level 3   | 0                                     | 0                             | 0                             | 0                 | 0                          | 0                    | 0      |
| Balance, end of period   | \$ 252                                | \$ 26                         | \$ 0                          | \$ 3              | \$ 59                      | \$ 1                 | \$ 341 |
| Changes in unrealized gains (losses) relating to Level 3 assets and liabilities still held at the end of the period included | \$ 0                                  | \$ 0                          | \$ 0                          | \$ 0              | \$ 123                     | \$ (1 )              | \$ 122 |

in realized  
investment gains  
(losses)

<sup>(1)</sup> Derivative assets and liabilities are presented net

Three Months Ended  
June 30, 2015

| (In millions)  | Fixed Maturities                                   |                                     | Perpetual                           | Equity     | Derivatives <sup>(1)</sup> |                              |                            |       |
|--|--|-------------------------------------|-------------------------------------|------------|----------------------------|------------------------------|----------------------------|-------|
|  | Mortgage-<br>and<br>Asset-<br>Backed<br>Securities | Banks/<br>Financial<br>Institutions | Banks/<br>Financial<br>Institutions | Securities | Securities                 | Foreign<br>Currency<br>Swaps | Credit<br>Default<br>Swaps | Total |
| Balance, beginning of period   | \$221  | \$ 26                               | \$ 150                              | \$ 3       | \$(283)                    | \$ 1                         | \$118                      |       |
| Realized investment gains (losses) included in earnings  | 0  | 0                                   | 0                                   | 0          | 58                         | 0                            | 58                         |       |
| Unrealized gains (losses) included in other comprehensive income (loss)  | (6 )   | (1 )                                | (3 )                                | 0          | 2                          | 0                            | (8 )                       |       |
| Purchases, issuances, sales and settlements:   |  |                                     |                                     |            |                            |                              |                            |       |
| Purchases  | 0  | 0                                   | 0                                   | 0          | 0                          | 0                            | 0                          |       |
| Issuances  | 0  | 0                                   | 0                                   | 0          | 0                          | 0                            | 0                          |       |
| Sales  | 0  | 0                                   | (147 )                              | 0          | 0                          | 0                            | (147 )                     |       |
| Settlements  | (1 )   | 0                                   | 0                                   | 0          | 0                          | 0                            | (1 )                       |       |
| Transfers into Level 3   | 0  | 0                                   | 0                                   | 0          | 0                          | 0                            | 0                          |       |
| Transfers out of Level 3   | 0  | 0                                   | 0                                   | 0          | 0                          | 0                            | 0                          |       |
| Balance, end of period   | \$214  | \$ 25                               | \$ 0                                | \$ 3       | \$(223)                    | \$ 1                         | \$20                       |       |
| Changes in unrealized gains (losses) relating to Level 3 assets and liabilities still held at the end of the period included in realized investment gains (losses) | \$0  | \$ 0                                | \$ 0                                | \$ 0       | \$58                       | \$ 0                         | \$58                       |       |

<sup>(1)</sup> Derivative assets and liabilities are presented net



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Six Months Ended  
June 30, 2016

| (In millions)  | Fixed Maturities   | Perpetual Equity                    | Derivatives <sup>(1)</sup> |                                  |                  |            |
|--|--|-------------------------------------|----------------------------|----------------------------------|------------------|------------|
|  | Mortgage-<br>and Banks/<br>Asset- Financial<br>Backed Institutions<br>Securities | Banks/<br>Financial<br>Institutions | Securities                 | Foreign Credit<br>Currency Swaps | Default<br>Swaps | Total      |
| Balance, beginning of period   | \$220  | \$ 26                               | \$ 0                       | \$ 3                             | \$(192)          | \$ 1 \$58  |
| Realized investment gains (losses) included in earnings  | 0  | 0                                   | 0                          | 0                                | 268              | 0 268      |
| Unrealized gains (losses) included in other comprehensive income (loss)  | 47   | 0                                   | 0                          | 0                                | (16 )            | 0 31       |
| Purchases, issuances, sales and settlements:   |  |                                     |                            |                                  |                  |            |
| Purchases  | 0  | 0                                   | 0                          | 0                                | 0                | 0 0        |
| Issuances  | 0  | 0                                   | 0                          | 0                                | 0                | 0 0        |
| Sales  | 0  | 0                                   | 0                          | 0                                | 0                | 0 0        |
| Settlements  | (15 )  | 0                                   | 0                          | 0                                | (1 )             | 0 (16 )    |
| Transfers into Level 3   | 0  | 0                                   | 0                          | 0                                | 0                | 0 0        |
| Transfers out of Level 3   | 0  | 0                                   | 0                          | 0                                | 0                | 0 0        |
| Balance, end of period   | \$252  | \$ 26                               | \$ 0                       | \$ 3                             | \$59             | \$ 1 \$341 |
| Changes in unrealized gains (losses) relating to Level 3 assets and liabilities still held at the end of the period included in realized investment gains (losses) | \$0  | \$ 0                                | \$ 0                       | \$ 0                             | \$268            | \$ 0 \$268 |

<sup>(1)</sup> Derivative assets and liabilities are presented net

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Six Months Ended  
June 30, 2015

| (In millions)  | Fixed Maturities   | Perpetual Equity                    | Equity                              | Derivatives <sup>(1)</sup>       |                  |       |         |
|--|--|-------------------------------------|-------------------------------------|----------------------------------|------------------|-------|---------|
|  | Mortgage-<br>and Banks/<br>Asset- Financial<br>Backed Institutions<br>Securities | Banks/<br>Financial<br>Institutions | Banks/<br>Financial<br>Institutions | Foreign Credit<br>Currency Swaps | Default<br>Swaps | Total |         |
| Balance, beginning of period   | \$223  | \$ 26                               | \$ 149                              | \$ 3                             | \$(212)          | \$ 0  | \$189   |
| Realized investment gains (losses) included in earnings  | 0  | 0                                   | 0                                   | 0                                | (25 )            | 1     | (24 )   |
| Unrealized gains (losses) included in other comprehensive income (loss)  | (7 )   | (1 )                                | (2 )                                | 0                                | (2 )             | 0     | (12 )   |
| Purchases, issuances, sales and settlements:   |  |                                     |                                     |                                  |                  |       |         |
| Purchases  | 0  | 0                                   | 0                                   | 0                                | 0                | 0     | 0       |
| Issuances  | 0  | 0                                   | 0                                   | 0                                | 0                | 0     | 0       |
| Sales  | 0  | 0                                   | (147 )                              | 0                                | 0                | 0     | (147 )  |
| Settlements  | (2 )   | 0                                   | 0                                   | 0                                | 16               | 0     | 14      |
| Transfers into Level 3   | 0  | 0                                   | 0                                   | 0                                | 0                | 0     | 0       |
| Transfers out of Level 3   | 0  | 0                                   | 0                                   | 0                                | 0                | 0     | 0       |
| Balance, end of period   | \$214  | \$ 25                               | \$ 0                                | \$ 3                             | \$(223)          | \$ 1  | \$20    |
| Changes in unrealized gains (losses) relating to Level 3 assets and liabilities still held at the end of the period included in realized investment gains (losses) | \$0  | \$ 0                                | \$ 0                                | \$ 0                             | \$(25 )          | \$ 1  | \$(24 ) |

<sup>(1)</sup> Derivative assets and liabilities are presented net

## Fair Value Sensitivity

## Level 3 Significant Unobservable Input Sensitivity

The following tables summarize the significant unobservable inputs used in the valuation of our Level 3 available-for-sale investments and derivatives. Included in the tables are the inputs or range of possible inputs that have an effect on the overall valuation of the financial instruments.

June 30, 2016

| (In millions)   | Fair Value           | Valuation Technique(s) | Unobservable Input     | Range (Weighted Average) |        |
|---|----------------------|------------------------|------------------------|--------------------------|--------|
| Assets:   |                      |                        |                        |                          |        |
| Securities available for sale, carried at fair value: |                      |                        |                        |                          |        |
| Fixed maturities:                                     |                      |                        |                        |                          |        |
| Mortgage- and asset-backed securities                 | \$252                | Consensus pricing      | Offered quotes         | N/A                      | (d)    |
| Banks/financial institutions                          | 26                   | Consensus pricing      | Offered quotes         | N/A                      | (d)    |
| Equity securities                                     | 3                    | Net asset value        | Offered quotes         | \$1 - \$793 (\$9)        |        |
| Other assets:   |                      |                        |                        |                          |        |
| Foreign currency swaps                                | 42                   | Discounted cash flow   | Interest rates (USD)   | 1.36% - 1.83%            | (a)    |
|   |                      |                        | Interest rates (JPY)   | (.04%) - .17%            | (b)    |
|   |                      |                        | CDS spreads            | 20 - 163 bps             |        |
|   |                      |                        | Foreign exchange rates | 21.14%                   | (c)    |
|   | 61                   | Discounted cash flow   | Interest rates (USD)   | 1.64% - 2.14%            | (a)    |
|   |                      |                        | Interest rates (JPY)   | .15% - .60%              | (b)    |
|   |                      |                        | CDS spreads            | 19 - 106 bps             |        |
|   | 73                   | Discounted cash flow   | Interest rates (USD)   | 1.64% - 2.14%            | (a)    |
|   |                      |                        | Interest rates (JPY)   | .15% - .60%              | (b)    |
|   |                      |                        | Foreign exchange rates | 21.14%                   | (c)    |
|   |                      |                        | Base correlation       | 64.18% - 69.87%          | (e)    |
|   | Credit default swaps | 1                      | Discounted cash flow   | CDS spreads              | 84 bps |
| Recovery rate   |                      |                        |                        | 36.93%                   |        |
|   |                      |                        |                        |                          |        |
| Total assets  | \$458                |                        |                        |                          |        |

(a) Inputs derived from U.S. long-term rates to accommodate long maturity nature of our swaps

(b) Inputs derived from Japan long-term rates to accommodate long maturity nature of our swaps

(c) Based on 10 year volatility of JPY/USD exchange rate

(d) N/A represents securities where we receive unadjusted broker quotes and for which there is no transparency into the providers' valuation techniques or unobservable inputs.

(e) Range of base correlation for our bespoke tranche for attachment and detachment points corresponding to market indices.

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June 30, 2016

| (In millions)          | Fair Value | Valuation Technique(s) | Unobservable Input     | Range (Weighted Average) |     |
|------------------------|------------|------------------------|------------------------|--------------------------|-----|
| <b>Liabilities:</b>    |            |                        |                        |                          |     |
| Foreign currency swaps | \$96       | Discounted cash flow   | Interest rates (USD)   | 1.64% - 2.14%            | (a) |
|                        |            |                        | Interest rates (JPY)   | .15% - .60%              | (b) |
|                        |            |                        | CDS spreads            | 32 - 147 bps             |     |
|                        |            |                        | Foreign exchange rates | 21.14%                   | (c) |
|                        | 19         | Discounted cash flow   | Interest rates (USD)   | 1.64% - 2.14%            | (a) |
|                        |            |                        | Interest rates (JPY)   | .15% - .60%              | (b) |
|                        |            |                        | CDS spreads            | 49 - 329 bps             |     |
|                        | 2          | Discounted cash flow   | Interest rates (USD)   | 1.64% - 2.14%            | (a) |
|                        |            |                        | Interest rates (JPY)   | .15% - .60%              | (b) |
|                        |            |                        | Foreign exchange rates | 21.14%                   | (c) |
| Total liabilities      | \$117      |                        |                        |                          |     |

(a) Inputs derived from U.S. long-term rates to accommodate long maturity nature of our swaps

(b) Inputs derived from Japan long-term rates to accommodate long maturity nature of our swaps

(c) Based on 10 year volatility of JPY/USD exchange rate

December 31, 2015

| (In millions)   | Fair Value | Valuation Technique(s) | Unobservable Input     | Range (Weighted Average) |     |
|---|------------|------------------------|------------------------|--------------------------|-----|
| Assets:   |            |                        |                        |                          |     |
| Securities available for sale, carried at fair value: |            |                        |                        |                          |     |
| Fixed maturities:                                     |            |                        |                        |                          |     |
| Mortgage- and asset-backed securities                 | \$220      | Consensus pricing      | Offered quotes         | N/A                      | (d) |
| Banks/financial institutions                          | 26         | Consensus pricing      | Offered quotes         | N/A                      | (d) |
| Equity securities                                     | 3          | Net asset value        | Offered quotes         | \$1-\$677 (\$7)          |     |
| Other assets:   |            |                        |                        |                          |     |
| Foreign currency swaps                                | 7          | Discounted cash flow   | Interest rates (USD)   | 2.20% - 2.62%            | (a) |
|   |            |                        | Interest rates (JPY)   | .42% - 1.22%             | (b) |
|   |            |                        | CDS spreads            | 32 - 147 bps             |     |
|   |            |                        | Foreign exchange rates | 20.05%                   | (c) |
|   | 94         | Discounted cash flow   | Interest rates (USD)   | 2.20% - 2.62%            | (a) |
|   |            |                        | Interest rates (JPY)   | .42% - 1.22%             | (b) |
|   |            |                        | Foreign exchange rates | 20.05%                   | (c) |
|   |            |                        | Base correlation       | 53.26% - 58.40%          | (e) |
| Credit default swaps                                  | 1          | Discounted cash flow   | CDS spreads            | 123 bps                  |     |
|   |            |                        | Recovery rate          | 36.87%                   |     |
|   |            |                        |                        |                          |     |
| Total assets  | \$351      |                        |                        |                          |     |

(a) Inputs derived from U.S. long-term rates to accommodate long maturity nature of our swaps

(b) Inputs derived from Japan long-term rates to accommodate long maturity nature of our swaps

(c) Based on 10 year volatility of JPY/USD exchange rate

(d) N/A represents securities where we receive unadjusted broker quotes and for which there is no transparency into the providers' valuation techniques or unobservable inputs.

(e) Range of base correlation for our bespoke tranche for attachment and detachment points corresponding to market indices

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December 31, 2015

| (In millions)          | Fair Value | Valuation Technique(s) | Unobservable Input     | Range (Weighted Average) |     |
|------------------------|------------|------------------------|------------------------|--------------------------|-----|
| <b>Liabilities:</b>    |            |                        |                        |                          |     |
| Foreign currency swaps | \$158      | Discounted cash flow   | Interest rates (USD)   | 2.20% - 2.62%            | (a) |
|                        |            |                        | Interest rates (JPY)   | .42% - 1.22%             | (b) |
|                        |            |                        | CDS spreads            | 32 - 147 bps             |     |
|                        |            |                        | Foreign exchange rates | 20.05%                   | (c) |
|                        | 120        | Discounted cash flow   | Interest rates (USD)   | 2.20% - 2.62%            | (a) |
|                        |            |                        | Interest rates (JPY)   | .42% - 1.22%             | (b) |
|                        |            |                        | CDS spreads            | 35 - 213 bps             |     |
|                        | 15         | Discounted cash flow   | Interest rates (USD)   | 2.20% - 2.62%            | (a) |
|                        |            |                        | Interest rates (JPY)   | .42% - 1.22%             | (b) |
|                        |            |                        | Foreign exchange rates | 20.05%                   | (c) |
| Total liabilities      | \$293      |                        |                        |                          |     |

(a) Inputs derived from U.S. long-term rates to accommodate long maturity nature of our swaps

(b) Inputs derived from Japan long-term rates to accommodate long maturity nature of our swaps

(c) Based on 10 year volatility of JPY/USD exchange rate

The following is a discussion of the significant unobservable inputs or valuation techniques used in determining the fair value of securities and derivatives classified as Level 3.

#### Net Asset Value

We hold certain unlisted equity securities whose fair value is derived based on the financial statements published by the investee. These securities do not trade on an active market and the valuations derived are dependent on the availability of timely financial reporting of the investee. Net asset value is an unobservable input in the determination of fair value of equity securities.

#### Offered Quotes

In circumstances where our valuation model price is overridden because it implies a value that is not consistent with current market conditions, we will solicit bids from a limited number of brokers. We also receive unadjusted prices from brokers for our mortgage and asset-backed securities. These quotes are non-binding but are reflective of valuation best estimates at that particular point in time. Offered quotes are an unobservable input in the determination of fair value of mortgage- and asset-backed securities, certain banks/financial institutions, certain other corporate, and equity securities investments.

#### Interest Rates, CDS Spreads, Foreign Exchange Rates

The significant drivers of the valuation of the interest and foreign exchange swaps are interest rates, foreign exchange rates and CDS spreads. Our swaps have long maturities that increase the sensitivity of the swaps to interest rate fluctuations. Since most of our yen-denominated cross currency swaps are in a net liability position, an increase in interest rates will decrease the liabilities and increase the value of the swap.

Foreign exchange swaps also have a lump-sum final settlement of foreign exchange principal receivables at the termination of the swap. An increase in yen interest rates will decrease the value of the final settlement foreign exchange receivables and decrease the value of the swap, and an increase in U.S. dollar interest rates will increase the swap value.

A similar sensitivity pattern is observed for the foreign exchange rates. When the spot U.S. dollar/Japanese yen (USD/JPY) foreign exchange rate decreases and the swap is receiving a final exchange payment in JPY, the swap value will increase due to the appreciation of the JPY. Most of our swaps are designed to receive payments in JPY at the termination and will thus be impacted by the USD/JPY foreign exchange rate in this way. In cases where there is no final foreign exchange receivable in JPY and we are paying JPY as interest payments and receiving USD, a decrease in the foreign exchange rate will lead to a decrease in the swap value.

The extinguisher feature in most of our swaps results in a cessation of cash flows and no further payments between the parties to the swap in the event of a default on the referenced or underlying collateral. To price this feature, we apply the survival probability of the referenced entity to the projected cash flows. The survival probability uses the CDS spreads and recovery rates to adjust the present value of the cash flows. For extinguisher swaps with positive values, an increase in CDS spreads decreases the likelihood of receiving the final exchange payments and reduces the value of the swap.

Due to the long duration of these swaps and the need to extrapolate from short-term observable data to derive and measure long-term inputs, certain inputs, assumptions and judgments are required to value future cash flows that cannot be corroborated by current inputs or current observable market data.

Interest rates, CDS spreads, and foreign exchange rates are unobservable inputs in the determination of fair value of foreign currency swaps.

Base Correlations, CDS Spreads, Recovery Rates

Our remaining CDO is a tranche on a basket of single-name credit default swaps. The risk in this synthetic CDO comes from the single-name CDS risk and the correlations between the single names. The valuation of synthetic CDOs is dependent on the calibration of market prices for interest rates, single name CDS default probabilities and base correlation using financial modeling tools. Since there is limited or no observable data available for this tranche, the base correlations must be obtained from commonly traded market tranches such as the CDX and iTraxx indices. From the historical prices of these indices, base correlations can be obtained to develop a pricing curve of CDOs with different seniorities. Since the reference entities of the market indices do not match those in the portfolio underlying the synthetic



CDO to be valued, several processing steps are taken to map the CDO in our portfolio to the indices. With the base correlation determined and the appropriate spreads selected, a valuation is calculated. An increase in the CDS spreads in the underlying portfolio leads to a decrease in the value due to higher probability of defaults and losses. The impact on the valuation due to base correlation depends on a number of factors, including the riskiness between market tranches and the modeled tranche based on our portfolio and the equivalence between detachment points in these tranches. Generally speaking, an increase in base correlation will decrease the value of the senior tranches while increasing the value of junior tranches. This may result in a positive or negative value change.

The CDO tranche in our portfolio is a senior mezzanine tranche and, due to the low level of credit support for this type of tranche, exhibits equity-like behavior. As a result, an increase in recovery rates tends to cause its value to decrease.

Base correlations, CDS spreads, and recovery rates are unobservable inputs in the determination of fair value of credit default swaps.

For additional information on our investments and financial instruments, see the accompanying Notes 1, 3 and 4 and Notes 1, 3 and 4 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015.

## 6. REINSURANCE

We enter into fixed quota-share coinsurance agreements with other companies in the normal course of business. For each of our reinsurance agreements, we determine whether the agreement provides indemnification against loss or liability relating to insurance risk in accordance with applicable accounting standards. Reinsurance premiums and benefits paid or provided are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Premiums and benefits are reported net of insurance ceded.

We have recorded a deferred profit liability related to reinsurance transactions. The remaining deferred profit liability of \$953 million, as of June 30, 2016, included in future policy benefits in the consolidated balance sheet, is being amortized into income over the expected lives of the policies. We also have recorded a reinsurance recoverable for reinsurance transactions, which is included in other assets in the consolidated balance sheet and had a remaining balance of \$959 million and \$805 million as of June 30, 2016 and December 31, 2015, respectively. The increase in the reinsurance recoverable balance was driven by two aggregating factors: yen strengthening and the growth in reserves related to the business that has been reinsured as the policies age. The spot yen/dollar exchange rate strengthened by approximately 17% and ceded reserves increased approximately 2% from December 31, 2015 to June 30, 2016.

The following table reconciles direct premium income and direct benefits and claims to net amounts after the effect of reinsurance.

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| (In millions)  | Three Months Ended |         | Six Months Ended |         |
|--|--------------------|---------|------------------|---------|
|  | June 30,           |         | June 30,         |         |
|  | 2016               | 2015    | 2016             | 2015    |
| Direct premium income                                      | \$4,915            | \$4,448 | \$9,605          | \$8,962 |
| Ceded to other companies:                                  |                    |         |                  |         |
| Ceded Aflac Japan closed blocks                            | (141 )             | (132 )  | (275 )           | (222 )  |
| Other  | (12 )              | (8 )    | (24 )            | (18 )   |
| Assumed from other companies:                              |                    |         |                  |         |
| Retrocession activities                                    | 59                 | 55      | 115              | 70      |
| Other  | 2                  | 1       | 4                | 4       |
| Net premium income   | \$4,823            | \$4,364 | \$9,425          | \$8,796 |
| Direct benefits and claims                                 | \$3,332            | \$3,013 | \$6,435          | \$6,038 |
| Ceded benefits and change in reserves for future benefits: |                    |         |                  |         |
| Ceded Aflac Japan closed blocks                            | (129 )             | (120 )  | (250 )           | (200 )  |
| Other  | 8                  | 10      | 12               | 3       |
| Assumed from other companies:                              |                    |         |                  |         |
| Retrocession activities                                    | 56                 | 51      | 109              | 65      |
| Other  | (13 )              | (17 )   | (27 )            | (17 )   |
| Benefits and claims, net                                   | \$3,254            | \$2,937 | \$6,279          | \$5,889 |

These reinsurance transactions are indemnity reinsurance that do not relieve us from our obligations to policyholders. In the event that the reinsurer is unable to meet their obligations, we remain liable for the reinsured claims.

As a part of our capital contingency plan, we entered into a committed reinsurance facility agreement on December 1, 2015 in the amount of approximately 110 billion yen. This reinsurance facility agreement is effective from December 1, 2015 until December 31, 2016. There are also additional commitment periods of a one-year duration each which are automatically extended unless notification is received from the reinsurer within 60 days prior to the expiration. The reinsurer can withdraw from the committed facility if Aflac's Standard and Poor's (S&P) rating drops below BBB-. As of June 30, 2016, we have not executed a reinsurance treaty under this committed reinsurance facility.

## 7. NOTES PAYABLE

A summary of notes payable follows:

| (In millions)   | June 30,<br>2016     | December 31,<br>2015  |
|---|----------------------|-----------------------|
| 2.65% senior notes due February 2017                            | \$650 <sup>(1)</sup> | \$ 651 <sup>(1)</sup> |
| 2.40% senior notes due March 2020                               | 547 <sup>(2)</sup>   | 546 <sup>(2)</sup>    |
| 4.00% senior notes due February 2022                            | 348                  | 348                   |
| 3.625% senior notes due June 2023                               | 696                  | 696                   |
| 3.625% senior notes due November 2024                           | 744                  | 744                   |
| 3.25% senior notes due March 2025                               | 445                  | 445                   |
| 6.90% senior notes due December 2039                            | 394 <sup>(2)</sup>   | 393 <sup>(2)</sup>    |
| 6.45% senior notes due August 2040                              | 445                  | 445                   |
| 5.50% subordinated debentures due September 2052                | 486                  | 486                   |
| Yen-denominated Uridashi notes:                                 |                      |                       |
| 2.26% notes due September 2016 (principal amount 8 billion yen) | 78                   | 66                    |
| Yen-denominated Samurai notes:                                  |                      |                       |
| 1.84% notes due July 2016 (principal amount 15.8 billion yen)   | 154 <sup>(3)</sup>   | 131                   |
| Capitalized lease obligations payable through 2023              | 22                   | 20                    |
| Total notes payable   | \$5,009              | \$ 4,971              |

<sup>(1)</sup> Principal amount plus an issuance premium that is being amortized over the life of the notes

<sup>(2)</sup> Principal amount net of an issuance discount that is being amortized over the life of the notes

<sup>(3)</sup> Paid off in July 2016 at its specific maturity date

Prior-year amounts have been adjusted for the adoption of accounting guidance on January 1, 2016 related to debt issuance costs.

In March 2016, the Parent Company entered into a three-year senior unsecured revolving credit facility agreement with a group of financial institutions that provides for borrowings of up to 100.0 billion yen on a revolving basis. Borrowings bear interest at a rate per annum equal to the Tokyo interbank market rate (TIBOR) plus, at our option, either (a) the applicable TIBOR margin during the period from the closing date to the commitment termination date or (b) the applicable TIBOR margin during the term out period. The applicable margin ranges between .35% and .75% during the period from the closing date to the commitment termination date and .70% and 1.50% during the term out period, depending on the Parent Company's debt ratings as of the date of determination. In addition, the Parent Company is required to pay a facility fee on the commitments ranging between .30% and .50%, also based on the Parent Company's debt ratings as of the date of determination. Borrowings under this credit agreement may be used for general corporate purposes, including a capital contingency plan for the operations of the Parent Company, and will expire on the earlier of (a) March 31, 2019, or (b) the date the commitments are terminated pursuant to an event of default, as such term is defined in the credit agreement. The credit facility requires compliance with certain financial covenants on a quarterly basis. As of June 30, 2016, we did not have any borrowings outstanding under our 100.0 billion yen revolving credit agreement.

The Parent Company and Aflac have a 364-day uncommitted bilateral line of credit with a third party that provides for borrowings in the amount of \$100 million. Borrowings will bear interest at the rate quoted by the bank and agreed upon at the time of making such loan and will have a three-month maturity period. There are no related facility fees, upfront expenses or financial covenant requirements. Borrowings under this credit agreement may be used for general corporate purposes. Borrowings under the financing agreement will mature no later than three months after the last drawdown date of October 15, 2016. As of June 30, 2016, we did not have any borrowings outstanding under our \$100 million credit agreement.

The Parent Company and Aflac have a five-year senior unsecured revolving credit facility agreement with a syndicate of financial institutions that provides for borrowings of up to 55.0 billion yen or the equivalent of yen in U.S. dollars on a revolving basis. This credit agreement provides for borrowings in Japanese yen or the equivalent of Japanese yen in U.S. dollars on a revolving basis. Borrowings bear interest at a rate per annum equal to, at our option, either (a) a eurocurrency rate determined by reference to the London Interbank Offered Rate (LIBOR) for the interest period relevant to such borrowing adjusted for certain additional costs or (b) a base rate determined by reference to the highest of (1) the federal funds effective rate plus  $\frac{1}{2}$  of 1%, (2) the rate of interest for such day announced by Mizuho Bank, Ltd. as its prime rate

and (3) the eurocurrency rate for an interest period of one month plus 1.00%, in each case plus an applicable margin. The applicable margin ranges between .79% and 1.275% for eurocurrency rate borrowings and 0.0% and .275% for base rate borrowings, depending on the Parent Company's debt ratings as of the date of determination. In addition, the Parent Company and Aflac are required to pay a facility fee on the commitments ranging between .085% and .225%, also based on the Parent Company's debt ratings as of the date of determination. Borrowings under the amended and restated credit facility may be used for general corporate purposes, including a capital contingency plan for the operations of the Parent Company and Aflac. The amended and restated credit facility requires compliance with certain financial covenants on a quarterly basis and will expire on the earlier of (a) September 18, 2020, or (b) the date the commitments are terminated pursuant to an event of default, as such term is defined in the credit agreement. As of June 30, 2016, we did not have any borrowings outstanding under our 55.0 billion yen revolving credit agreement.

The Parent Company and Aflac have an uncommitted bilateral line of credit with a third party that provides for borrowings in the amount of \$50 million. Borrowings will bear interest at the rate quoted by the bank and agreed upon at the time of making such loan and will have a three-month maturity period. There are no related facility fees, upfront expenses or financial covenant requirements. Borrowings under this credit agreement may be used for general corporate purposes. As of June 30, 2016, we did not have any borrowings outstanding under our \$50 million credit agreement.

We were in compliance with all of the covenants of our notes payable and lines of credit at June 30, 2016. No events of default or defaults occurred during the six-month period ended June 30, 2016.

For additional information, see Notes 4 and 9 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015.

## 8. SHAREHOLDERS' EQUITY

The following table is a reconciliation of the number of shares of the Company's common stock for the six-month periods ended June 30.

| (In thousands of shares)                                    | 2016    | 2015    |
|---|---------|---------|
| Common stock - issued:                                      |         |         |
| Balance, beginning of period                                | 669,723 | 668,132 |
| Exercise of stock options and issuance of restricted shares | 1,041   | 934     |
| Balance, end of period                                      | 670,764 | 669,066 |
| Treasury stock:   |         |         |
| Balance, beginning of period                                | 245,343 | 225,687 |
| Purchases of treasury stock:                                |         |         |
| Open market   | 16,026  | 13,534  |
| Other   | 224     | 214     |
| Dispositions of treasury stock:                             |         |         |
| Shares issued to AFL Stock Plan                             | (594 )  | (611 )  |
| Exercise of stock options                                   | (238 )  | (265 )  |
| Other   | (112 )  | (110 )  |
| Balance, end of period                                      | 260,649 | 238,449 |
| Shares outstanding, end of period                           | 410,115 | 430,617 |

Outstanding share-based awards are excluded from the calculation of weighted-average shares used in the computation of basic earnings per share (EPS). The following table presents the approximate number of share-based awards to purchase shares, on a weighted-average basis, that were considered to be anti-dilutive and were excluded from the calculation of diluted earnings per share for the following periods.

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|                                  | Three<br>Months<br>Ended<br>June 30, |       | Six Months<br>Ended<br>June 30, |       |
|----------------------------------|--------------------------------------|-------|---------------------------------|-------|
| (In thousands)                   | 2016                                 | 2015  | 2016                            | 2015  |
| Anti-dilutive share-based awards | 696                                  | 1,390 | 1,689                           | 1,634 |

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## Share Repurchase Program

During the first six months of 2016, we repurchased 16.0 million shares of our common stock in the open market for \$1.0 billion as part of our share repurchase program. During the first six months of 2015, we repurchased 13.5 million shares of our common stock in the open market for \$833 million as part of our share repurchase program. As of June 30, 2016, a remaining balance of 32.3 million shares of our common stock was available for purchase under share repurchase authorizations by our board of directors.

## Reclassifications from Accumulated Other Comprehensive Income

The tables below are reconciliations of accumulated other comprehensive income by component for the following periods.

## Changes in Accumulated Other Comprehensive Income

## Three Months Ended

June 30, 2016

| (In millions)  | Unrealized<br>Foreign<br>Currency<br>Translation<br>Gains<br>(Losses) | Unrealized<br>Gains<br>(Losses)<br>on<br>Investment<br>Securities | Unrealized<br>Gains<br>(Losses)<br>on<br>Derivatives | Pension<br>Liability<br>Adjustment | Total    |
|--|---|---|--|------------------------------------|----------|
| Balance, beginning of period   | \$ (1,584 )   | \$ 4,684  | \$ (24 )   | \$ (140 )                          | \$ 2,936 |
| Other comprehensive<br>income (loss) before<br>reclassification                  | 737   | 1,750   | 5  | (4 )                               | 2,488    |
| Amounts reclassified from<br>accumulated other<br>comprehensive income<br>(loss) | 0   | 7   | 0  | 1                                  | 8        |
| Net current-period other<br>comprehensive<br>income (loss)                       | 737   | 1,757   | 5  | (3 )                               | 2,496    |
| Balance, end of period   | \$ (847 )   | \$ 6,441  | \$ (19 )   | \$ (143 )                          | \$ 5,432 |

All amounts in the table above are net of tax.

## Three Months Ended

June 30, 2015

| (In millions)   | Unrealized<br>Foreign<br>Currency<br>Translation<br>Gains<br>(Losses) | Unrealized<br>Gains<br>(Losses)<br>on<br>Investment<br>Securities | Unrealized<br>Gains<br>(Losses)<br>on<br>Derivatives | Pension<br>Liability<br>Adjustment | Total    |
|---|---|---|--|------------------------------------|----------|
| Balance, beginning of period                                    | \$ (2,540 )   | \$ 5,026  | \$ (28 )   | \$ (126 )                          | \$ 2,332 |
| Other comprehensive<br>income (loss) before<br>reclassification | (185 )  | (1,598 )  | 1  | 0                                  | (1,782 ) |
|   | 0   | (44 )   | 0  | 1                                  | (43 )    |

Amounts reclassified from  
accumulated other  
comprehensive income  
(loss)

|  |            |          |          |           |          |
|--|------------|----------|----------|-----------|----------|
| Net current-period other<br>comprehensive<br>income (loss) | (185 )     | (1,642 ) | 1        | 1         | (1,825 ) |
| Balance, end of period                                     | \$(2,725 ) | \$ 3,384 | \$ (27 ) | \$ (125 ) | \$ 507   |

All amounts in the table above are net of tax.



Six Months Ended  
June 30, 2016

| (In millions)  | Unrealized<br>Foreign<br>Currency<br>Translation<br>Gains<br>(Losses) | Unrealized<br>Gains<br>(Losses)<br>on<br>Investment<br>Securities | Unrealized<br>Gains<br>(Losses)<br>on<br>Derivatives | Pension<br>Liability<br>Adjustment | Total   |
|--|---|---|--|------------------------------------|---------|
| Balance, beginning of period   | \$ (2,196 )   | \$ 2,986  | \$ (26 )   | \$ (139 )                          | \$625   |
| Other comprehensive<br>income (loss) before<br>reclassification                  | 1,349   | 3,498   | 7  | (5 )                               | 4,849   |
| Amounts reclassified from<br>accumulated other<br>comprehensive income<br>(loss) | 0   | (43 )   | 0  | 1                                  | (42 )   |
| Net current-period other<br>comprehensive<br>income (loss)                       | 1,349   | 3,455   | 7  | (4 )                               | 4,807   |
| Balance, end of period   | \$ (847 )   | \$ 6,441  | \$ (19 )   | \$ (143 )                          | \$5,432 |

All amounts in the table above are net of tax.

Six Months Ended  
June 30, 2015

| (In millions)  | Unrealized<br>Foreign<br>Currency<br>Translation<br>Gains<br>(Losses) | Unrealized<br>Gains<br>(Losses)<br>on<br>Investment<br>Securities | Unrealized<br>Gains<br>(Losses)<br>on<br>Derivatives | Pension<br>Liability<br>Adjustment | Total    |
|--|---|---|--|------------------------------------|----------|
| Balance, beginning of period   | \$ (2,541 )   | \$ 4,672  | \$ (26 )   | \$ (126 )                          | \$1,979  |
| Other comprehensive<br>income (loss) before<br>reclassification                  | (184 )  | (1,211 )  | (1 )   | 0                                  | (1,396 ) |
| Amounts reclassified from<br>accumulated other<br>comprehensive income<br>(loss) | 0   | (77 )   | 0  | 1                                  | (76 )    |
| Net current-period other<br>comprehensive<br>income (loss)                       | (184 )  | (1,288 )  | (1 )   | 1                                  | (1,472 ) |
| Balance, end of period   | \$ (2,725 )   | \$ 3,384  | \$ (27 )   | \$ (125 )                          | \$507    |

All amounts in the table above are net of tax.

The tables below summarize the amounts reclassified from each component of accumulated other comprehensive income based on source for the following periods.

## Reclassifications Out of Accumulated Other Comprehensive Income

| (In millions)  | Three Months<br>Ended<br>June 30, 2016<br>Amount<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Income | Affected Line Item in the<br>Statements of Earnings  |
|--|---|--|
| Details about Accumulated Other Comprehensive Income<br>Components |   |  |
| Unrealized gains (losses) on available-for-sale<br>securities      | \$ 22   | Sales and redemptions                                |
|  | (33 )   | Other-than-temporary impairment<br>losses realized   |
|  | (11 )   | Total before tax                                     |
|  | 4   | Tax (expense) or benefit <sup>(1)</sup>              |
|  | \$ (7 )   | Net of tax   |
| Amortization of defined benefit pension items:                     |   |  |
| Actuarial gains (losses)   | \$ (5 )   | Acquisition and operating<br>expenses <sup>(2)</sup> |
| Prior service (cost) credit  | 3   | Acquisition and operating<br>expenses <sup>(2)</sup> |
|  | 1   | Tax (expense) or benefit <sup>(1)</sup>              |
|  | \$ (1 )   | Net of tax   |
| Total reclassifications for the period                             | \$ (8 )   | Net of tax   |

<sup>(1)</sup> Based on 35% tax rate

<sup>(2)</sup> These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 10 for additional details).

| (In millions)  | Three Months<br>Ended<br>June 30, 2015<br>Amount<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Income | Affected Line Item in the<br>Statements of Earnings |
|--|---|---|
| Details about Accumulated Other Comprehensive Income<br>Components |   |   |
| Unrealized gains (losses) on available-for-sale<br>securities      | \$ 68   | Sales and redemptions                               |
|  | 0   | Other-than-temporary impairment<br>losses realized  |
|  | 68  | Total before tax                                    |
|  | (24 )   | Tax (expense) or benefit <sup>(1)</sup>             |
|  | \$ 44   | Net of tax  |
| Amortization of defined benefit pension items:                     |   |   |
| Actuarial gains (losses)   | \$ (5 )   |   |

|  |         |   |
|--|---------|---|
|  |         | Acquisition and operating expenses <sup>(2)</sup> |
| Prior service (cost) credit            | 4       | Acquisition and operating expenses <sup>(2)</sup> |
|  | 0       | Tax (expense) or benefit <sup>(1)</sup>           |
|  | \$ (1 ) | Net of tax  |
| Total reclassifications for the period | \$ 43   | Net of tax  |

<sup>(1)</sup> Based on 35% tax rate

<sup>(2)</sup> These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 10 for additional details).

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| (In millions)   | Six Months<br>Ended<br>June 30, 2016<br>Amount<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Income | Affected Line Item in the<br>Statements of Earnings |
|---|---|---|
| Details about Accumulated Other Comprehensive Income Components |   |   |
| Unrealized gains (losses) on available-for-sale securities      | \$ 113  | Sales and redemptions                               |
|   | (47 )   | Other-than-temporary impairment losses realized     |
|   | 66  | Total before tax                                    |
|   | (23 )   | Tax (expense) or benefit <sup>(1)</sup>             |
|   | \$ 43   | Net of tax  |
| Amortization of defined benefit pension items:                  |   |   |
| Actuarial gains (losses)  | \$ (8 )   | Acquisition and operating expenses <sup>(2)</sup>   |
| Prior service (cost) credit                                     | 6   | Acquisition and operating expenses <sup>(2)</sup>   |
|   | 1   | Tax (expense) or benefit <sup>(1)</sup>             |
|   | \$ (1 )   | Net of tax  |
| Total reclassifications for the period                          | \$ 42   | Net of tax  |

<sup>(1)</sup> Based on 35% tax rate

<sup>(2)</sup> These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 10 for additional details).

| (In millions)   | Six Months<br>Ended<br>June 30, 2015<br>Amount<br>Reclassified<br>from<br>Accumulated<br>Other<br>Comprehensive<br>Income | Affected Line Item in the<br>Statements of Earnings |
|---|---|---|
| Details about Accumulated Other Comprehensive Income Components |   |   |
| Unrealized gains (losses) on available-for-sale securities      | \$ 124  | Sales and redemptions                               |
|   | (6 )  | Other-than-temporary impairment losses realized     |
|   | 118   | Total before tax                                    |
|   | (41 )   | Tax (expense) or benefit <sup>(1)</sup>             |
|   | \$ 77   | Net of tax  |
| Amortization of defined benefit pension items:                  |   |   |
| Actuarial gains (losses)  | \$ (9 )   | Acquisition and operating expenses <sup>(2)</sup>   |
| Prior service (cost) credit                                     | 8   |   |

|  |         |   |
|--|---------|---|
|  |         | Acquisition and operating expenses <sup>(2)</sup> |
|  | 0       | Tax (expense) or benefit <sup>(1)</sup>           |
|  | \$ (1 ) | Net of tax  |
| Total reclassifications for the period | \$ 76   | Net of tax  |

<sup>(1)</sup> Based on 35% tax rate

<sup>(2)</sup> These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 10 for additional details).

## 9. SHARE-BASED COMPENSATION

As of June 30, 2016, the Company had outstanding share-based awards under two long-term incentive compensation plans.

The first plan, which expired in February 2007, is a stock option plan which allowed grants for incentive stock options (ISOs) to employees and non-qualifying stock options (NQSOs) to employees and non-employee directors. The options have a term of 10 years. The exercise price of options granted under this plan is equal to the fair market value of a share of the Company's common stock at the date of grant. Options granted before the plan's expiration date remain outstanding in accordance with their terms.

The second long-term incentive compensation plan allows awards to Company employees for ISOs, NQSOs, restricted stock, restricted stock units, and stock appreciation rights. Non-employee directors are eligible for grants of NQSOs, restricted stock, and stock appreciation rights. The ISOs and NQSOs have a term of 10 years, and the share-based awards generally vest upon time-based conditions or time- and performance-based conditions. Time-based vesting generally occurs after three years. Performance-based vesting conditions generally include the attainment of goals related to Company financial performance. As of June 30, 2016, approximately 8.9 million shares were available for future grants under this plan, and the only performance-based awards issued and outstanding were restricted stock awards.

Share-based awards granted to U.S.-based grantees are settled with authorized but unissued Company stock, while those issued to Japan-based grantees are settled with treasury shares.

The following table provides information on stock options outstanding and exercisable at June 30, 2016.

|             | Stock<br>Option Shares<br>(in thousands) | Weighted-Average<br>Remaining Term<br>(in years) | Aggregate<br>Intrinsic<br>Value<br>(in millions) | Weighted-Average<br>Exercise Price Per<br>Share |
|-------------|--|--|--|---|
| Outstanding | 7,282                                    | 4.7  | \$ 146   | \$ 52.10  |
| Exercisable | 5,369                                    | 3.3  | 125  | 48.92   |

We received cash from the exercise of stock options in the amount of \$33 million during the first six months of 2016, compared with \$31 million in the first six months of 2015. The tax benefit realized as a result of stock option exercises and restricted stock releases was \$18 million in the first six months of 2016, compared with \$19 million in the first six months of 2015.

As of June 30, 2016, total compensation cost not yet recognized in our financial statements related to restricted stock awards was \$44 million, of which \$12 million (474 thousand shares) was related to restricted stock awards with a performance-based vesting condition. We expect to recognize these amounts over a weighted-average period of approximately 1.5 years. There are no other contractual terms covering restricted stock awards once vested.

For additional information on our long-term share-based compensation plans and the types of share-based awards, see Note 12 of the Notes to the Consolidated Financial Statements included in our annual report to shareholders for the year ended December 31, 2015.

## 10. BENEFIT PLANS

We have funded defined benefit plans in Japan and the United States, which cover substantially all of our full-time employees. Additionally, we maintain non-qualified, unfunded supplemental retirement plans that provide defined pension benefits in excess of limits imposed by federal tax law for certain Japanese, U.S. and former employees. Effective October 1, 2013, the U.S. tax-qualified defined benefit plan was frozen to new employees hired on or after October 1, 2013 and to employees rehired on or after October 1, 2013. U.S. employees who are not participants in the defined benefit plan receive a nonelective 401(k) employer contribution. Additionally, effective January 1, 2015, the U.S. non-qualified supplemental retirement plan was frozen to new participants.

We provide certain health care benefits for eligible U.S. retired employees, their beneficiaries and covered dependents ("other postretirement benefits"). The health care plan is contributory and unfunded. Effective January 1, 2014, employees eligible for benefits included the following: (1) active employees whose age plus service, in years, equaled or exceeded 80 (rule of 80); (2) active employees who were age 55 or older and have met the 15 years of service requirement; (3) active employees who would meet the rule of 80 in the next five years; (4) active employees who

were age 55 or older and who would meet the 15 years of service requirement within the next five years; and (5) current retirees. For certain employees and former employees, additional coverage is provided for all medical expenses for life.

Pension and other postretirement benefit expenses, included in acquisition and operating expenses in the consolidated statement of earnings, included the following components:

| (In millions)                               | Three Months Ended June 30, |      |      |      |                               |       |
|---|-----------------------------|------|------|------|-------------------------------|-------|
|   | Pension Benefits            |      |      |      | Other Postretirement Benefits |       |
|   | Japan                       |      | U.S. |      | 2016                          | 2015  |
|   | 2016                        | 2015 | 2016 | 2015 | 2016                          | 2015  |
| Components of net periodic benefit cost:    |                             |      |      |      |                               |       |
| Service cost                                | \$4                         | \$3  | \$6  | \$6  | \$0                           | \$0   |
| Interest cost                               | 1                           | 1    | 8    | 8    | 1                             | 0     |
| Expected return on plan assets              | (1)                         | (1)  | (5)  | (5)  | 0                             | 0     |
| Amortization of net actuarial loss          | 1                           | 1    | 3    | 3    | 1                             | 1     |
| Amortization of prior service cost (credit) | 0                           | 0    | 0    | 0    | (3)                           | (4)   |
| Net periodic (benefit) cost                 | \$5                         | \$4  | \$12 | \$12 | \$(1)                         | \$(3) |

| (In millions)                               | Six Months Ended June 30, |      |      |      |                               |       |
|---|---------------------------|------|------|------|-------------------------------|-------|
|   | Pension Benefits          |      |      |      | Other Postretirement Benefits |       |
|   | Japan                     |      | U.S. |      | 2016                          | 2015  |
|   | 2016                      | 2015 | 2016 | 2015 | 2016                          | 2015  |
| Components of net periodic benefit cost:    |                           |      |      |      |                               |       |
| Service cost                                | \$8                       | \$7  | \$12 | \$12 | \$0                           | \$0   |
| Interest cost                               | 3                         | 3    | 16   | 16   | 1                             | 1     |
| Expected return on plan assets              | (2)                       | (2)  | (11) | (11) | 0                             | 0     |
| Amortization of net actuarial loss          | 1                         | 1    | 6    | 7    | 1                             | 1     |
| Amortization of prior service cost (credit) | 0                         | 0    | 0    | 0    | (6)                           | (8)   |
| Net periodic (benefit) cost                 | \$10                      | \$9  | \$23 | \$24 | \$(4)                         | \$(6) |

During the six months ended June 30, 2016, Aflac Japan contributed approximately \$11 million (using the weighted-average yen/dollar exchange rate for the six-month period ending June 30, 2016) to the Japanese funded defined benefit plan, and Aflac U.S. did not make a contribution to the U.S. funded defined benefit plan.

For additional information regarding our Japanese and U.S. benefit plans, see Note 14 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015.

## 11. COMMITMENTS AND CONTINGENT LIABILITIES

We are a defendant in various lawsuits considered to be in the normal course of business. Members of our senior legal and financial management teams review litigation on a quarterly and annual basis. The final results of any litigation cannot be predicted with certainty. Although some of this litigation is pending in states where large punitive damages, bearing little relation to the actual damages sustained by plaintiffs, have been awarded in recent years, we believe the outcome of pending litigation will not have a material adverse effect on our financial position, results of operations, or cash flows.



As of June 30, 2016, we had commitments of \$72 million to fund potential future loan originations related to our investment in middle market loans. These commitments are contingent upon the availability of middle market loans that meet our underwriting criteria. In addition, we had commitments of \$177 million to fund potential future loan originations related to our investment in commercial mortgage loans. These commitments are contingent on the final underwriting and due diligence to be performed, and may or may not be funded. See Note 3 of the Notes to the Consolidated Financial Statements for more details on these investment programs.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

FORWARD-LOOKING INFORMATION

The Private Securities Litigation Reform Act of 1995 provides a “safe harbor” to encourage companies to provide prospective information, so long as those informational statements are identified as forward-looking and are accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those included in the forward-looking statements. We desire to take advantage of these provisions. This report contains cautionary statements identifying important factors that could cause actual results to differ materially from those projected herein, and in any other statements made by Company officials in communications with the financial community and contained in documents filed with the Securities and Exchange Commission (SEC). Forward-looking statements are not based on historical information and relate to future operations, strategies, financial results or other developments. Furthermore, forward-looking information is subject to numerous assumptions, risks and uncertainties. In particular, statements containing words such as “expect,” “anticipate,” “believe,” “goal,” “objective,” “may,” “should,” “estimate,” “intends,” “projects,” “will,” “assumes,” “potential,” “target” or similar words, as well as specific projections of future results, generally qualify as forward-looking. Aflac undertakes no obligation to update such forward-looking statements.

We caution readers that the following factors, in addition to other factors mentioned from time to time, could cause actual results to differ materially from those contemplated by the forward-looking statements:

- difficult conditions in global capital markets and the economy
- governmental actions for the purpose of stabilizing the financial markets
- defaults and credit downgrades of securities in our investment portfolio
- exposure to significant interest rate risk
- concentration of business in Japan
- limited availability of acceptable yen-denominated investments
- failure to comply with restrictions on patient privacy and information security
- foreign currency fluctuations in the yen/dollar exchange rate
- deviations in actual experience from pricing and reserving assumptions
- subsidiaries' ability to pay dividends to Aflac Incorporated
- ability to continue to develop and implement improvements in information technology systems
- concentration of our investments in any particular single-issuer or sector
- decline in creditworthiness of other financial institutions
- ability to attract and retain qualified sales associates and employees
- differing judgments applied to investment valuations
- significant valuation judgments in determination of amount of impairments taken on our investments
- credit and other risks associated with Aflac's investment in perpetual securities
- decreases in our financial strength or debt ratings
- inherent limitations to risk management policies and procedures
- extensive regulation and changes in law or regulation by governmental authorities
- interruption in telecommunication, information technology and other operational systems, or a failure to maintain the security, confidentiality or privacy of sensitive data residing on such systems
- catastrophic events including, but not necessarily limited to, epidemics, pandemics, tornadoes, hurricanes, earthquakes, tsunamis, acts of terrorism and damage incidental to such events
- changes in U.S. and/or Japanese accounting standards
- ability to effectively manage key executive succession
- level and outcome of litigation
- increased expenses and reduced profitability resulting from changes in assumptions for pension and other postretirement benefit plans

ongoing changes in our industry

loss of consumer trust resulting from events external to our operations

failure of internal controls or corporate governance policies and procedures

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## MD&A OVERVIEW

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to inform the reader about matters affecting the financial condition and results of operations of Aflac Incorporated and its subsidiaries for the three- and six-month periods ended June 30, 2016 and 2015, respectively. Results of operations for interim periods are not necessarily indicative of results for the entire year. As a result, the following discussion should be read in conjunction with the consolidated financial statements and notes that are included in our annual report to shareholders for the year ended December 31, 2015. This MD&A is divided into the following sections:

Our Business

Performance Highlights

Critical Accounting Estimates

Results of Operations, consolidated and by segment

Analysis of Financial Condition, including discussion of market risks of financial instruments

Capital Resources and Liquidity, including discussion of availability of capital and the sources and uses of cash

## OUR BUSINESS

Aflac Incorporated (the Parent Company) and its subsidiaries (collectively, the Company) primarily sell supplemental health and life insurance in the United States and Japan. The Company's insurance business is marketed and administered through American Family Life Assurance Company of Columbus (Aflac), which operates in the United States (Aflac U.S.) and as a branch in Japan (Aflac Japan). Most of Aflac's policies are individually underwritten and marketed through independent agents. Aflac U.S. markets and administers group products through Continental American Insurance Company (CAIC), branded as Aflac Group Insurance. Our insurance operations in the United States and our branch in Japan service the two markets for our insurance business.

## PERFORMANCE HIGHLIGHTS

Yen-denominated income statement accounts are translated to U.S. dollars using a weighted-average Japanese yen/U.S. dollar foreign exchange rate, while yen-denominated balance sheet accounts are translated to U.S. dollars using a spot Japanese yen/U.S. dollar foreign exchange rate. The spot yen/dollar exchange rate at June 30, 2016 was 102.91, or 17.2% stronger than the spot yen/dollar exchange rate of 120.61 at December 31, 2015. The weighted-average yen/dollar exchange rate for the three-month period ended June 30, 2016 was 108.28, or 11.9% stronger than the weighted-average yen/dollar exchange rate of 121.20 for the same period in 2015. The weighted-average yen/dollar exchange rate for the six-month period ended June 30, 2016 was 111.82, or 7.4% stronger than the weighted-average yen/dollar exchange rate of 120.14 for the same period in 2015.

Reflecting the stronger yen/dollar exchange rate, revenues were \$5.4 billion in the second quarter of 2016, compared with \$5.3 billion in the second quarter of 2015. Net earnings were \$548 million, or \$1.32 per diluted share, compared with \$573 million, or \$1.32 per diluted share, in the second quarter of 2015.

Also reflecting the stronger yen/dollar exchange rate, revenues were \$10.9 billion in the first six months of 2016, compared with \$10.5 billion in the first six months of 2015. Net earnings were \$1.3 billion, or \$3.06 per diluted share, compared with \$1.2 billion, or \$2.83 per diluted share, for the first six months of 2015.

Results in the second quarter of 2016 included pretax net realized investment losses of \$187 million (\$122 million after-tax), compared with net realized investment gains of \$127 million (\$83 million after-tax) in the second quarter of 2015. Net investment losses in the second quarter of 2016 included \$33 million (\$21 million after-tax) of other-than-temporary impairment losses; \$13 million of net gains (\$8 million after-tax) from the sale or redemption of securities; and \$167 million of net losses (\$109 million after-tax) from valuing derivatives.

Results in the first six months of 2016 included pretax net realized investment losses of \$114 million (\$74 million after-tax), compared with net realized investment gains of \$140 million (\$91 million after-tax) in the first six months of 2015. Net investment losses in the first six months of 2016 included \$47 million (\$31 million after-tax) of other-than-temporary impairment losses; \$104 million of net gains (\$68 million after-tax) from the sale or redemption of securities; and \$171 million of net losses (\$111 million after-tax) from valuing derivatives. Shareholders' equity included a net unrealized gain on investment securities and derivatives of \$6.4 billion at June 30, 2016, compared with a net unrealized gain of \$3.0 billion at December 31, 2015.

In March 2016, the Parent Company entered into a three-year senior unsecured revolving credit facility agreement with a syndicate of financial institutions that provides for borrowings of up to 100 billion yen. For further information regarding this transaction, see Note 7 of the Notes to the Consolidated Financial Statements and the Capital Resources and Liquidity section of this MD&A.

In the first six months of 2016, we repurchased 16.0 million shares of our common stock in the open market for \$1.0 billion under our share repurchase program.

#### CRITICAL ACCOUNTING ESTIMATES

We prepare our financial statements in accordance with U.S. generally accepted accounting principles (GAAP). These principles are established primarily by the Financial Accounting Standards Board (FASB). In this MD&A, references to U.S. GAAP issued by the FASB are derived from the FASB Accounting Standards Codification<sup>TM</sup>(ASC). The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates based on currently available information when recording transactions resulting from business operations. The estimates that we deem to be most critical to an understanding of Aflac's results of operations and financial condition are those related to the valuation of investments and derivatives, deferred policy acquisition costs (DAC), liabilities for future policy benefits and unpaid policy claims, and income taxes. The preparation and evaluation of these critical accounting estimates involve the use of various assumptions developed from management's analyses and judgments. The application of these critical accounting estimates determines the values at which 93% of our assets and 79% of our liabilities are reported as of June 30, 2016, and thus has a direct effect on net earnings and shareholders' equity. Subsequent experience or use of other assumptions could produce significantly different results.

There have been no changes in the items that we have identified as critical accounting estimates during the six months ended June 30, 2016. For additional information, see the Critical Accounting Estimates section of MD&A included in our annual report to shareholders for the year ended December 31, 2015.

#### New Accounting Pronouncements

For information on new accounting pronouncements and the impact, if any, on our financial position or results of operations, see Note 1 of the Notes to the Consolidated Financial Statements.

#### RESULTS OF OPERATIONS

The following discussion includes references to our performance measures, operating earnings and operating earnings per diluted share, that are not based on U.S. GAAP. Operating earnings is the measure of segment profit or loss we use to evaluate segment performance and allocate resources. Consistent with U.S. GAAP accounting guidance for segment reporting, operating earnings is our measure of segment performance. Aflac believes that an analysis of operating earnings is vitally important to an understanding of our underlying profitability drivers and trends of our insurance business. Furthermore, because a significant portion of our business is conducted in Japan, we believe it is equally important to understand the impact of translating Japanese yen into U.S. dollars.

Aflac defines operating earnings (a non-U.S. GAAP financial measure) as the profits derived from operations. Operating earnings includes interest cash flows associated with notes payable but excludes items that cannot be predicted or that are outside of management's control, such as realized investment gains and losses from securities transactions, impairments, and derivative and hedging activities; nonrecurring items; and other non-operating income (loss) from net earnings. Aflac's derivative activities are primarily used to hedge foreign exchange and interest rate risk in our investment portfolio as well as manage foreign exchange risk for certain notes payable and forecasted cash flows denominated in yen. Our management uses operating earnings to evaluate the financial performance of Aflac's insurance operations because realized gains and losses from securities transactions, impairments, and derivative and hedging activities, as well as other and nonrecurring items, tend to be driven by general economic conditions and events or related to infrequent activities not directly associated with the Company's insurance operations, and therefore may obscure the underlying fundamentals and trends in Aflac's insurance operations.



The following table is a reconciliation of items impacting operating and net earnings and operating and net earnings per diluted share.

#### Reconciliation of Operating Earnings to Net Earnings

|  | In Millions                      |                   | Per Diluted Share |         | In Millions                    |                      | Per Diluted Share |         |
|--|----------------------------------|-------------------|-------------------|---------|--------------------------------|----------------------|-------------------|---------|
|  | Three Months Ended June 30, 2016 | 2015              | 2016              | 2015    | Six Months Ended June 30, 2016 | 2015                 | 2016              | 2015    |
| Operating earnings                                       | \$707                            | \$651             | \$ 1.71           | \$ 1.50 | \$1,433                        | \$1,329              | \$ 3.44           | \$ 3.04 |
| Items impacting net earnings, net of tax: <sup>(1)</sup> |                                  |                   |                   |         |                                |                      |                   |         |
| Realized investment gains (losses):                      |                                  |                   |                   |         |                                |                      |                   |         |
| Securities transactions and impairments                  | (13 )                            | 60                | (.03 )            | .14     | 37                             | 100                  | .08               | .23     |
| Impact of derivative and hedging activities:             |                                  |                   |                   |         |                                |                      |                   |         |
| Hedge costs related to foreign currency investments      | (31 )                            | (12 )             | (.08 )            | (.03 )  | (60 )                          | (21 )                | (.14 )            | (.05 )  |
| Other derivative and hedging activities                  | (91 ) <sup>(2)</sup>             | 20 <sup>(2)</sup> | (.22 )            | .05     | (79 ) <sup>(2)</sup>           | (14 ) <sup>(2)</sup> | (.19 )            | (.03 )  |
| Other and non-recurring income (loss)                    | (24 )                            | (146 )            | (.06 )            | (.34 )  | (52 )                          | (158 )               | (.13 )            | (.36 )  |
| Net earnings   | \$548                            | \$573             | \$ 1.32           | \$ 1.32 | \$1,279                        | \$1,236              | \$ 3.06           | \$ 2.83 |

<sup>(1)</sup> Reconciling items are calculated based on using a 35% tax rate

<sup>(2)</sup> Excludes a gain of \$14 and \$15, after tax, for the three-month periods and \$28 and \$26, after tax, for the six-month periods ended June 30, 2016 and 2015, respectively, related to the interest rate component of the change in fair value of foreign currency swaps on notes payable which is classified as an operating gain when analyzing segment operations

#### Realized Investment Gains and Losses

Our investment strategy is to invest primarily in fixed-maturity securities to provide a reliable stream of investment income, which is one of the drivers of the Company's growth and profitability. This investment strategy incorporates asset-liability matching (ALM) to align the expected cash flows of the portfolio to the needs of the Company's liability structure. We do not purchase securities with the intent of generating capital gains or losses. However, investment gains and losses may be realized as a result of changes in the financial markets and the creditworthiness of specific issuers, tax planning strategies, and/or general portfolio management and rebalancing. The realization of investment gains and losses is independent of the underwriting and administration of our insurance products, which are the principal drivers of our profitability.

#### Securities Transactions and Impairments

During the three-month period ended June 30, 2016, we realized pretax investment gains, net of losses, of \$13 million (\$8 million after-tax) from sales and redemptions of securities. We realized pretax investment losses of \$33 million (\$21 million after-tax) as a result of the recognition of other-than-temporary impairment losses on certain securities.

During the six-month period ended June 30, 2016, we realized pretax investment gains, net of losses, of \$104 million (\$68 million after-tax) from sales and redemptions of securities. We realized pretax investment losses of \$47 million (\$31 million after-tax) as a result of the recognition of other-than-temporary impairment losses on certain securities.

During the three-month period ended June 30, 2015, we realized pretax investment gains, net of losses, of \$92 million (\$60 million after-tax) from sales and redemptions of securities.



During the six-month period ended June 30, 2015, we realized pretax investment gains, net of losses, of \$160 million (\$104 million after-tax) from sales and redemptions of securities. We realized pretax investment losses of \$6

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million (\$4 million after-tax) as a result of the recognition of other-than-temporary impairment losses on certain securities.

See Note 3 of the Notes to the Consolidated Financial Statements for a more detailed discussion of these investment activities.

The following table details our pretax impairment losses by investment category.

| (In millions)  | Three    |      | Six      |      |
|--|----------|------|----------|------|
|  | Months   |      | Months   |      |
|  | Ended    |      | Ended    |      |
|  | June 30, |      | June 30, |      |
|  | 2016     | 2015 | 2016     | 2015 |
| Perpetual securities   | \$0      | \$ 0 | \$2      | \$ 0 |
| Corporate bonds  | 9        | 0    | 21       | 2    |
| Bank/financial institution bonds                                     | 0        | 0    | 0        | 4    |
| Equity securities  | 24       | 0    | 24       | 0    |
| Total other-than-temporary impairment losses realized <sup>(1)</sup> | \$33     | \$ 0 | \$47     | \$ 6 |

<sup>(1)</sup> Includes \$33 and an immaterial amount for the three-month periods and \$47 and \$6 for the six-month periods ended June 30, 2016 and 2015, respectively, from change in intent to sell securities or change in intent to hold securities until recovery

#### Impact of Derivative and Hedging Activities

Our derivative activities include foreign currency swaps and credit default swaps held in consolidated variable interest entities (VIEs); foreign currency forwards and options, interest rate swaptions and futures on certain fixed-maturity securities; foreign currency forwards and options that economically hedge certain portions of forecasted cash flows denominated in yen; and foreign currency swaps associated with certain senior notes and our subordinated debentures. During the three-month period ended June 30, 2016, we realized pretax investment losses, net of gains, of \$167 million (\$109 million after-tax), compared with pretax investment gains, net of losses, of \$35 million (\$23 million after-tax) for the same period in 2015, as a result of valuing these derivatives, net of the effects of hedge accounting. During the six-month period ended June 30, 2016, we realized pretax investment losses, net of gains, of \$171 million (\$111 million after-tax), compared with pretax investment losses, net of gains, of \$14 million (\$9 million after-tax) for the same period in 2015, as a result of valuing these derivatives, net of the effects of hedge accounting. For a description of other items that could be included in the Impact of Derivative and Hedging Activities, see the Hedging Activities subsection of MD&A and Note 4 of the accompanying Notes to the Consolidated Financial Statements.

For additional information regarding realized investment gains and losses, see Notes 3 and 4 of the Notes to the Consolidated Financial Statements.

#### Non-recurring Items

During the three- and six-month periods ended June 30, 2015, the make-whole premium paid to the investors of our 8.50% fixed-rate senior notes for the early redemption of those notes was recorded as a \$230 million pretax non-operating loss (\$150 million after-tax, or \$.35 per diluted share).

#### Foreign Currency Translation

Aflac Japan's premiums and most of its investment income are received in yen. Claims and expenses are paid in yen, and we have yen-denominated assets that support yen-denominated policy liabilities. These and other yen-denominated financial statement items are translated into dollars for financial reporting purposes. We translate Aflac Japan's yen-denominated income statement into dollars using an average exchange rate for the reporting period, and we translate its yen-denominated balance sheet using the exchange rate at the end of the period.

Due to the size of Aflac Japan, where our functional currency is the Japanese yen, fluctuations in the yen/dollar exchange rate can have a significant effect on our reported results. In periods when the yen weakens, translating yen

into dollars results in fewer dollars being reported. When the yen strengthens, translating yen into dollars results in more dollars being reported. Consequently, yen weakening has the effect of suppressing current period results in relation to the comparable prior period, while yen strengthening has the effect of magnifying current period results in relation to the comparable prior period. As a result, we view foreign currency translation as a financial reporting issue for Aflac rather than an economic event to our Company or shareholders. Because changes in exchange rates distort the growth rates of our operations, management evaluates Aflac's financial performance excluding the impact of foreign currency translation.

## Income Taxes

Our combined U.S. and Japanese effective income tax rate on pretax earnings was 34.3% for the three-month period ended June 30, 2016, compared with 34.5% for the same period in 2015. Our combined U.S. and Japanese effective income tax rate on pretax earnings was 34.4% for the six-month period ended June 30, 2016, compared with 34.5% for the same period in 2015.

## Earnings Guidance

Our objective for 2016 is to produce stable operating earnings per diluted share compared with 2015. In the second half of 2016, as we continue to focus on initiatives designed to drive future growth, our expectation is to increase spending, particularly related to promotional and information technology (IT) expenditures. With interest rates at significantly depressed levels, especially with negative interest rates in Japan, it is difficult to invest cash flows at attractive yields while maintaining a prudent risk tolerance. If we achieve our objective for 2016, the following table shows the likely results for operating earnings per diluted share, including the impact of foreign currency translation using various yen/dollar exchange rate scenarios.

2016 Operating Earnings Per Diluted Share Scenarios<sup>(1)</sup>

## Weighted-Average

| Yen/Dollar Exchange Rate | Operating Earnings Per Diluted Share | % Growth Over 2015 | Yen Impact |
|--------------------------|--------------------------------------|--------------------|------------|
| 100                      | \$6.85 - 7.09                        | 11.2 - 15.1 %      | \$ .68     |
| 105                      | 6.66 - 6.90                          | 8.1 - 12.0         | .49        |
| 110                      | 6.49 - 6.73                          | 5.4 - 9.3          | .32        |
| 115                      | 6.34 - 6.58                          | 2.9 - 6.8          | .17        |
| 120.99 <sup>(2)</sup>    | 6.17 - 6.41                          | .2 - 4.1           | .00        |
| 125                      | 6.07 - 6.31                          | (1.5 ) - 2.4       | (.10 )     |

<sup>(1)</sup> A non-GAAP measure that includes interest cash flows associated with notes payable but excludes realized investment gains/losses (securities transactions, impairments, and the impact of derivative and hedging activities), nonrecurring items, and other non-operating income (loss) from net earnings in 2016 and 2015. Due to the unpredictable and uncontrollable nature of these reconciling items, we do not calculate a GAAP equivalent of this earnings guidance metric.

<sup>(2)</sup> Actual 2015 weighted-average exchange rate

Using the 2015 average yen/dollar exchange rate of 120.99, our annual objective is to report operating earnings per diluted share of \$6.17 to \$6.41. If the yen/dollar exchange rate averages 100 to 110 for the third quarter of 2016, we would expect earnings in the third quarter to be approximately \$1.58 to \$1.86 per diluted share.

## INSURANCE OPERATIONS

Aflac's insurance business consists of two segments: Aflac Japan and Aflac U.S. Aflac Japan, which operates as a branch of Aflac, is the principal contributor to consolidated earnings. U.S. GAAP financial reporting requires that a company report financial and descriptive information about operating segments in its annual and interim period financial statements. Furthermore, we are required to report a measure of segment profit or loss, certain revenue and expense items, and segment assets.

We evaluate our sales efforts using new annualized premium sales, an industry operating measure. New annualized premium sales, which include both new sales and the incremental increase in premiums due to conversions, represent the premiums that we would collect over a 12-month period, assuming the policies remain in force. For Aflac Japan, new annualized premium sales are determined by applications submitted during the reporting period. For Aflac U.S.,

new annualized premium sales are determined by applications that are issued during the reporting period. Premium income, or earned premiums, is a financial performance measure that reflects collected or due premiums that have been earned ratably on policies in force during the reporting period.



revenues, and pretax operating earnings in yen terms. Excluding foreign currency changes from the prior period (a non-U.S. GAAP measure), U.S. dollar-denominated investment income accounted for approximately 50% of Aflac Japan's investment income during the first six months of 2016, compared with 45% a year ago.

The following table illustrates the effect of translating Aflac Japan's U.S. dollar-denominated investment income and related items into yen by comparing certain segment results with those that would have been reported had yen/dollar exchange rates remained unchanged from the comparable period in the prior year. In order to compare the current period to the prior period without the impact of foreign currency, the current period income statement is translated at the prior year's comparable period average exchange rate.

Aflac Japan Percentage Changes Over Previous Period

(Yen Operating Results)

For the Periods Ended June 30,

|  | Including Foreign<br>Currency Changes |        |            |       | Excluding Foreign<br>Currency Changes <sup>(2)</sup> |        |            |         |
|--|---------------------------------------|--------|------------|-------|--|--------|------------|---------|
|  | Three Months                          |        | Six Months |       | Three<br>Months                                      |        | Six Months |         |
|  | 2016                                  | 2015   | 2016       | 2015  | 2016   | 2015   | 2016       | 2015    |
| Net investment income                    | (5.4 )%                               | 5.7 %  | (3.6 )%    | 6.5 % | (.1 )%   | (2.5)% | (.1 )%     | (1.2 )% |
| Total operating revenues                 | .7                                    | .0     | .2         | .6    | 1.6  | (1.4)  | .8         | (.6 )   |
| Pretax operating earnings <sup>(1)</sup> | (1.0 )                                | (3.1 ) | (.9 )      | (.6 ) | 3.0  | (8.9)  | 1.6        | (5.9 )  |

<sup>(1)</sup> See the Insurance Operations section of this MD&A for our definition of segment operating earnings.

<sup>(2)</sup> Amounts excluding foreign currency changes on dollar-denominated items (a non-U.S. GAAP measure) were determined using the same yen/dollar exchange rate for the current period as the comparable period in the prior year. The following table presents a summary of operating ratios in yen terms for Aflac Japan.

|   | Three<br>Months<br>Ended<br>June 30, |        | Six Months<br>Ended<br>June 30, |        |
|---|--------------------------------------|--------|---------------------------------|--------|
|   | 2016                                 | 2015   | 2016                            | 2015   |
| Ratios to total revenues:                         |                                      |        |                                 |        |
| Benefits and claims, net                          | 60.5 %                               | 60.5 % | 60.2 %                          | 60.3 % |
| Operating expenses:                               |                                      |        |                                 |        |
| Amortization of deferred policy acquisition costs | 4.1                                  | 3.9    | 4.0                             | 4.0    |
| Insurance commissions                             | 4.9                                  | 5.0    | 4.9                             | 5.0    |
| Insurance and other expenses                      | 9.8                                  | 9.5    | 9.5                             | 9.1    |
| Total operating expenses                          | 18.8                                 | 18.4   | 18.4                            | 18.1   |
| Pretax operating earnings <sup>(1)</sup>          | 20.7                                 | 21.1   | 21.4                            | 21.6   |

<sup>(1)</sup> See the Insurance Operations section of this MD&A for our definition of segment operating earnings.

In the three- and six-month periods ended June 30, 2016, the benefit ratio remained relatively stable compared to the same respective period in the prior year, resulting from the impact of reinsurance and favorable claims experience, with some offset from the effects of currency translation. The three reinsurance agreements that we entered into since the end of the third quarter of 2013 reduced the benefit ratio by approximately 100 basis points for the three- and six-month periods ended June 30, 2016. In the three- and six-month periods ended June 30, 2016, the operating expense ratio increased primarily due to activities related to sales promotions, IT infrastructure enhancement and personnel. In total, the pretax operating profit margin remained relatively stable in the three- and six-month periods ended June 30, 2016, compared with the same periods in 2015. For the full year of 2016, we anticipate the pretax operating profit margin to be comparable with 2015 levels.

Aflac Japan Sales

The following table presents Aflac Japan's new annualized premium sales for the periods ended June 30.

|  | In Dollars   |       |            |       | In Yen       |      |            |      |
|--|--------------|-------|------------|-------|--------------|------|------------|------|
|  | Three Months |       | Six Months |       | Three Months |      | Six Months |      |
|  | 2016         | 2015  | 2016       | 2015  | 2016         | 2015 | 2016       | 2015 |
| (In millions of dollars and billions of yen) |              |       |            |       |              |      |            |      |
| New annualized premium sales                 | \$280        | \$252 | \$551      | \$478 | 30.3         | 30.6 | 61.4       | 57.6 |



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Increase (decrease) over prior period      11.2 % (8.0 )% 15.2 % (11.8)% (1.1 )% 9.4 % 6.7 % 3.7 %

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The following table details the contributions to new annualized premium sales by major insurance product for the periods ended June 30.

|                     | Three Months |        | Six Months |        |
|---------------------|--------------|--------|------------|--------|
|                     | 2016         | 2015   | 2016       | 2015   |
| Medical             | 27.9 %       | 24.7 % | 25.5 %     | 25.1 % |
| Cancer              | 46.0         | 41.0   | 40.7       | 41.2   |
| Ordinary life:      |              |        |            |        |
| Child endowment     | 5.1          | 7.9    | 7.1        | 9.0    |
| WAYS                | 13.5         | 18.3   | 19.4       | 15.2   |
| Other ordinary life | 6.0          | 6.1    | 5.8        | 6.6    |
| Other               | 1.5          | 2.0    | 1.5        | 2.9    |
| Total               | 100.0%       | 100.0% | 100.0%     | 100.0% |

The foundation of Aflac Japan's product portfolio has been, and continues to be, our third sector cancer and medical products. Sales of third sector products increased 11.2% during the second quarter and increased 6.4% in the first six months of 2016, compared with the same respective periods in 2015. We have been focusing more on promotion of our cancer and medical products in this low-interest-rate environment. These products are less interest-rate sensitive and more profitable compared to first sector products.

Cancer insurance sales were up 11.0% during the second quarter of 2016, compared with the same period in 2015. Aflac Japan enhanced its medical product with new riders in June 2015. This revision provides better protection against critical diseases such as cancer, heart attack and stroke. With continued cost pressure on Japan's health care system, we expect the need for third sector products will continue to rise in the future, and we remain convinced that the medical and cancer products Aflac Japan provides will continue to be an important part of our product portfolio. Recognizing the negative interest rate environment in Japan, we have taken actions to limit sales of Aflac Japan's first sector product sales, including WAYS and child endowment, that are gaining traction as first sector product sales were down 24.7% in the second quarter of 2016, compared to the same period in the prior year. As we continue to implement additional measures, we anticipate a sharp decline of at least 50% in first sector sales for the second half of the year. Our focus remains on less interest-sensitive third sector products.

We remain committed to selling through our traditional channels. These channels, consisting of affiliated corporate agencies, independent corporate agencies and individual agencies, accounted for 93.0% of total new annualized premium sales for Aflac Japan in the second quarter of 2016. During the three-month period ended June 30, 2016, we recruited 55 new sales agencies. At June 30, 2016, Aflac Japan was represented by approximately 12,600 sales agencies and more than 111,400 licensed sales associates employed by those agencies.

At June 30, 2016, we had agreements to sell our products at 370 banks, approximately 90% of the total number of banks in Japan. Bank channel sales accounted for 7.0% of new annualized premium sales in the second quarter of 2016 for Aflac Japan, compared with 14.6% during the second quarter of 2015.

Aflac Japan and Japan Post Holdings entered into a new agreement in July 2013, further expanding a partnership that was established in 2008 (see Japanese Regulatory Environment). At the end of June 2014, Japan Post Insurance (Kampo) received Financial Services Agency (FSA) regulatory approval to enter into an agency contract with Aflac Japan to begin distributing Aflac Japan's cancer insurance products at all of Kampo's 79 directly managed sales offices. Aflac Japan has developed a unique Aflac-branded cancer product for Japan Post and Kampo that was introduced on October 1, 2014. In the fourth quarter of 2014, the number of postal outlets selling our cancer products expanded to approximately 10,000, and starting July 1, 2015, Japan Post expanded the number of post offices that offer Aflac's cancer products to more than 20,000 postal outlets. We believe this alliance with Japan Post will further benefit our cancer insurance sales.

We believe that there is still a continued need for our products in Japan. Our sales target and focus in 2016 will continue to be centered around the sale of Aflac Japan's third sector products, including cancer and medical. Although our traditional channels remain key to our success, we have developed partnerships with new channels to help increase our overall sales growth. These channels include Japan Post, and we are making steady progress with our sales

through postal outlets. For the full year 2016, we anticipate that third sector sales will be in the range of down 3% to up 2%

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compared with 2015. We continue to believe that the long-term compound annual growth rate for third sector sales will be in the range of 4% to 6%.

#### Japanese Regulatory Environment

In 2015, the government of Japan staged an Initial Public Offering (IPO) for Japan Post Bank (JPB), Japan Post Insurance (JPI), and Japan Post Holdings (JPH) pursuant to legislation aimed at privatizing Japan's postal system (i.e., Japan Post).

In 2007, Aflac Japan was selected by Japan Post as its provider of cancer insurance to be sold through its post offices. In 2008, we began selling cancer insurance through these post offices. Japan Post has historically been a popular place for consumers to purchase insurance products. In July 2013, Aflac Japan entered into a new agreement with Japan Post Holdings to further expand a partnership that was established in 2008 (see Aflac Japan Sales).

In June 2013, a revision to the Financial Instruments and Exchange Act established a post-funded Orderly Resolution Regime for financial institutions to prevent a financial crisis in the event of a financial institution's failure. This regime came into effect in March 2014, but is not expected to have a material impact on the Company's operations in Japan.

#### Aflac Japan Investments

The level of investment income in yen is affected by available cash flow from operations, the timing of investing the cash flow, yields on new investments, the effect of yen/dollar exchange rates on U.S. dollar-denominated investment income, and other factors.

As part of our portfolio management and asset allocation process, Aflac Japan invests in U.S. dollar-denominated securities. Aflac Japan has been investing in U.S. dollar-denominated publicly-traded investment grade and below investment grade corporate fixed-maturity securities, and has entered into foreign currency forwards and options to hedge the currency risk on the fair value of the U.S. dollar securities. In 2015, Aflac Japan increased its allocation to U.S. dollar-denominated investments, including senior secured bank loans and high yield corporate bonds, and initiated a commercial mortgage loan investment program. In the first six months of 2016, Aflac Japan invested an additional \$535 million in its senior secured bank loan program and invested \$165 million in commercial mortgage loans. As of June 30, 2016, we had \$177 million in outstanding commitments to fund commercial mortgage loans. These commitments are contingent on the final underwriting and due diligence to be performed. In addition, starting in the first quarter of 2016, Aflac Japan initiated an allocation to a dividend-focused U.S. public equities program. In the first six months of 2016, Aflac Japan invested \$425 million in these U.S. public equities, which are classified as available for sale and carried on our balance sheet at fair value.

Starting in 2015, we increased Aflac Japan's investment in dividend-focused yen-denominated publicly traded equity securities, including investments in exchange traded funds (ETFs) holding Japan real estate investment trusts. In the first six months of 2016, Aflac Japan invested \$141 million in yen-denominated publicly traded equity securities, which are classified as available for sale and carried on our balance sheet at fair value.

See the Analysis of Financial Condition section of this MD&A for further discussion of these investment programs, and see Note 3 of the Notes to the Consolidated Financial Statements and Notes 1 and 3 of Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015 for more information regarding loans and loans receivables.

The following table presents the results of Aflac Japan's investment yields for the periods ended June 30.

|  | Three Months        |                     | Six Months          |                     |
|--|---------------------|---------------------|---------------------|---------------------|
|  | 2016 <sup>(1)</sup> | 2015 <sup>(1)</sup> | 2016 <sup>(1)</sup> | 2015 <sup>(1)</sup> |
| New money yield <sup>(2)</sup>   | 1.67 %              | 3.87 %              | 1.92 %              | 3.88 %              |
| Return on average invested assets, net of investment expenses <sup>(3)</sup>                 | 2.69                | 2.89                | 2.74                | 2.87                |
| Portfolio book yield, including dollar-denominated investments, end of period <sup>(2)</sup> | 2.71 %              | 2.83 %              | 2.71 %              | 2.83 %              |

<sup>(1)</sup>Yields are reported before the cost of foreign currency forwards that hedge foreign exchange risk of U.S.

dollar-denominated publicly

traded corporate bonds.

<sup>(2)</sup> Includes fixed maturities and perpetual securities, loan receivables, and equities

<sup>(3)</sup> Net of investment expenses, year-to-date number reflected on a quarterly average basis

On January 1, 2016, the company revised its definition of purchases to include "swap" purchase activity. New purchases include all purchases related to fixed maturities and perpetuals, loan receivables, and equities. Securities lending/repurchase agreement activity and capital contributions to alternatives are excluded. The definition of new money yield has also been revised to reflect this change. Yields for equities are based on the assumed dividend yield at the time of purchase. Historical amounts have been revised to reflect the new definitions.

The decrease in the Aflac Japan new money yield in the three- and six-month periods ended June 30, 2016 was primarily due to the front-loaded allocation to Japan Government Bonds (JGBs) and other high quality yen-denominated investments.

See Notes 3, 4 and 5 of the Notes to the Consolidated Financial Statements and the Analysis of Financial Condition section of this MD&A for additional information on our investments and hedging strategies.

#### AFLAC U.S. SEGMENT

##### Aflac U.S. Pretax Operating Earnings

Changes in Aflac U.S. pretax operating earnings and profit margins are primarily affected by morbidity, mortality, expenses, persistency and investment yields. The following table presents a summary of operating results for Aflac U.S.

##### Aflac U.S. Summary of Operating Results

|   | Three Months |         | Six Months |         |   |
|---|--------------|---------|------------|---------|---|
|   | Ended        |         | Ended      |         |   |
| (In millions)                                     | June 30,     |         | June 30,   |         |   |
|   | 2016         | 2015    | 2016       | 2015    |   |
| Net premium income                                | \$1,362      | \$1,331 | \$2,729    | \$2,670 |   |
| Net investment income                             | 176          | 168     | 350        | 334     |   |
| Other income                                      | 0            | 2       | 3          | 5       |   |
| Total operating revenues                          | 1,538        | 1,501   | 3,082      | 3,009   |   |
| Benefits and claims                               | 743          | 715     | 1,433      | 1,426   |   |
| Operating expenses:                               |              |         |            |         |   |
| Amortization of deferred policy acquisition costs | 117          | 113     | 258        | 241     |   |
| Insurance commissions                             | 147          | 146     | 294        | 293     |   |
| Insurance and other expenses                      | 240          | 234     | 474        | 471     |   |
| Total operating expenses                          | 504          | 493     | 1,026      | 1,005   |   |
| Total benefits and expenses                       | 1,247        | 1,208   | 2,459      | 2,431   |   |
| Pretax operating earnings <sup>(1)</sup>          | \$291        | \$293   | \$623      | \$578   |   |
| Percentage change over previous period:           |              |         |            |         |   |
| Net premium income                                | 2.2          | % 1.6   | % 2.2      | % 2.5   | % |
| Net investment income                             | 4.4          | 4.0     | 4.7        | 3.7     |   |

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|  |       |        |     |        |
|--|-------|--------|-----|--------|
| Total operating revenues                 | 2.5   | 1.9    | 2.4 | 2.8    |
| Pretax operating earnings <sup>(1)</sup> | (.3 ) | (2.0 ) | 8.0 | (4.1 ) |

<sup>(1)</sup> See the Insurance Operations section of this MD&A for our definition of segment operating earnings.

Annualized premiums in force increased 2.4% to \$5.8 billion at June 30, 2016, compared with \$5.6 billion at June 30, 2015.

The following table presents a summary of operating ratios for Aflac U.S.

|   | Three<br>Months<br>Ended<br>June 30, |        | Six Months<br>Ended<br>June 30, |        |
|---|--------------------------------------|--------|---------------------------------|--------|
|   | 2016                                 | 2015   | 2016                            | 2015   |
| Ratios to total revenues:                         |                                      |        |                                 |        |
| Benefits and claims                               | 48.3 %                               | 47.7 % | 46.5 %                          | 47.4 % |
| Operating expenses:                               |                                      |        |                                 |        |
| Amortization of deferred policy acquisition costs | 7.6                                  | 7.5    | 8.4                             | 8.0    |
| Insurance commissions                             | 9.5                                  | 9.7    | 9.5                             | 9.7    |
| Insurance and other expenses                      | 15.6                                 | 15.6   | 15.3                            | 15.7   |
| Total operating expenses                          | 32.7                                 | 32.8   | 33.2                            | 33.4   |
| Pretax operating earnings <sup>(1)</sup>          | 19.0                                 | 19.5   | 20.3                            | 19.2   |

<sup>(1)</sup>See the Insurance Operations section of this MD&A for our definition of segment operating earnings.

The benefit ratio in the three-month period ended June 30, 2016, increased compared with the same period in 2015 due to refinement in reserve items. The benefit ratio in the six-month period ended June 30, 2016, decreased compared with the same period in 2015 due to better claims experience in the first quarter of 2016. The operating expense ratio remained relatively stable during the three- and six-month periods ended June 30, 2016, compared with the same periods in 2015. In total, the pretax operating profit margin declined in the three-month period and improved in the six-month period ended June 30, 2016, compared with the same periods in 2015. For the remainder of 2016, we expect the benefit and expense ratios to be relatively stable compared with 2015.

#### Aflac U.S. Sales

The following table presents Aflac's U.S. new annualized premium sales for the periods ended June 30.

|                                       | Three Months |       | Six Months |       |
|---------------------------------------|--------------|-------|------------|-------|
| (In millions)                         | 2016         | 2015  | 2016       | 2015  |
| New annualized premium sales          | \$347        | \$344 | \$675      | \$660 |
| Increase (decrease) over prior period | 1.0 %        | 3.1 % | 2.3 %      | 1.4 % |

The following table details the contributions to new annualized premium sales by major insurance product category for the periods ended June 30.

|                              | Three Months |         | Six Months |         |
|------------------------------|--------------|---------|------------|---------|
|                              | 2016         | 2015    | 2016       | 2015    |
| Income-loss protection:      |              |         |            |         |
| Short-term disability        | 23.3 %       | 24.4 %  | 23.4 %     | 24.0 %  |
| Life                         | 5.6          | 5.5     | 5.6        | 5.8     |
| Asset-loss protection:       |              |         |            |         |
| Accident                     | 30.1         | 29.6    | 30.0       | 29.3    |
| Critical care <sup>(1)</sup> | 21.3         | 20.9    | 21.3       | 21.0    |
| Supplemental medical:        |              |         |            |         |
| Hospital indemnity           | 14.3         | 13.9    | 14.2       | 14.2    |
| Dental/vision                | 5.4          | 5.7     | 5.5        | 5.7     |
| Total                        | 100.0 %      | 100.0 % | 100.0 %    | 100.0 % |

<sup>(1)</sup> Includes cancer, critical illness, and hospital intensive care products

New annualized premium sales for accident insurance, our leading product category, increased 2.8%, short-term disability sales decreased 3.4%, critical care insurance sales (including cancer insurance) increased 2.8%, and hospital indemnity insurance sales increased 4.2% in the second quarter of 2016, compared with the same period in 2015.





In the second quarter of 2016, our traditional U.S. sales forces included more than 9,000 U.S. associates who were actively producing business on a weekly basis. We believe that the average weekly producing sales associates metric allows our sales management to actively monitor progress and needs on a real-time basis. Beyond expanding the size and capabilities of our traditional sales force, we remain encouraged about establishing and developing relationships with insurance brokers that typically handle the larger-case market.

The addition of group products has expanded our reach and enabled us to generate more sales opportunities with larger employers, brokers, and our traditional sales agents. We anticipate that the appeal of our group products will continue to enhance our opportunities to connect with larger businesses and their employees. Our portfolio of group and individual products offers businesses the opportunity to give their employees a more valuable and comprehensive selection of benefit options.

We believe that changes we made to our career and broker management infrastructure over the last 18 months are laying the foundation for expanded long-term growth opportunities. During 2014, Aflac U.S. implemented tactical initiatives centered around providing competitive compensation to our career agent sales hierarchy and positioning us to more effectively and consistently execute on the U.S. sales strategy across all states. These measures are designed to more effectively link sales management's success to Aflac's success. For example, we enhanced compensation through an incentive bonus for the first level of our sales management, district sales coordinators, who are primarily responsible for selling Aflac products and training new sales associates. Additionally, we eliminated the commission-based position of state sales coordinator. To better manage our state operations, we introduced the new position of market director, effective October 1, 2014. Market directors are salaried with the opportunity to earn sales-related bonuses. We believe these changes have enhanced and will continue to enhance performance management and better align compensation with new business results.

One Day Pay<sup>SM</sup> is a claims initiative that we have focused on at Aflac U.S. to process, approve and pay eligible claims in just one day. We believe that along with our brand and relevant products, this claims practice will help Aflac stand out from competitors.

With the evolving business market and the coverage standardization that will result from health care reform in the United States, we believe Aflac's voluntary products will become more relevant than ever. Our products provide cash benefits that can be used to help with increasing out-of-pocket medical expenses, help cover household costs, or protect against income and asset loss. Our group products and relationships with insurance brokers that handle the larger-case market are helping us as we expand our reach selling to larger businesses. We are regularly evaluating the marketplace to identify opportunities to bring the most relevant, cost-effective products to our customers. We believe the need for our products remains very strong, and we continue to work on enhancing our distribution capabilities to access employers of all sizes, including initiatives that benefit our field force and the broker community. At the same time, we are seeking opportunities to leverage our brand strength and attractive product portfolio in the evolving health care environment. While sales in the second quarter of 2016 were below our expectations, for the full year 2016 our objective is for Aflac U.S. new annualized premium sales to increase in the range of 3% to 5%. We anticipate the achievement of our annual U.S. sales target will be increasingly reliant on fourth quarter 2016 production as more of our business comes from larger employers that have fourth quarter enrollments.

#### U.S. Regulatory Environment

The Affordable Care Act (ACA) is intended to give Americans of all ages and income levels access to comprehensive major medical health insurance. The major elements of the bill became effective on January 1, 2014. The primary subject of the legislation is major medical insurance; as enacted, the ACA does not materially affect the design of our insurance products. However, indirect consequences of the legislation and regulations, including uncertainty related to implementation, could present challenges and/or opportunities that could potentially have an impact on our sales model, financial condition and results of operations. Our experience with Japan's national health care environment leads us to believe that the need for supplemental insurance will only increase over the coming years.

On December 18, 2015, the president signed into law the Consolidated Appropriations Act which included a revision to delay implementation of the Excise Tax on High Cost Plans, better known as the "Cadillac tax." This tax was originally scheduled to begin in 2017, was previously delayed until 2018, and is now scheduled to begin in 2020. The tax consists of 40% of the cost of employer sponsored health coverage in excess of certain dollar thresholds. In general, only Aflac specified disease and fixed indemnity (i.e. supplemental health) products offered on a pre-tax basis are taken into account under this tax.

The legislation also makes the tax deductible by the payer. If employers fund coverage on a pre-tax basis, Aflac, as the insurer, would be liable for its pro-rata share of any tax on excess coverage, determined based on the cost of Aflac coverage compared to the total cost of the applicable health coverage in which each employee is enrolled. Making the tax deductible would then reduce the economic impact of any tax that is imposed and payable by Aflac.

Many employers are concerned about the tax and what impact it will have on benefit offerings in the future. There is confusion in the market about how the tax is calculated and who pays the tax, presenting a risk that some employers will mistakenly conclude that all supplemental health products are included in the calculation for the tax regardless of pre-tax funding status or whether an employer's health coverage exceeds the trigger for the tax. Some employers may decide simply to drop coverage of affected supplemental health products, rather than convert it to an after-tax basis. During this extended implementation period, Aflac will be assessing the impact of this tax; educating employers about the tax; and investigating ways to mitigate the impact of the tax. Having employees pay for the coverage on an after-tax basis would exempt affected supplemental health products from the tax.

The Dodd-Frank Act, which was signed into law in 2010, created, among other things, a Financial Stability Oversight Council (the Council). In April 2012, the Council released a final rule describing the general process it will follow in determining whether to designate a nonbank financial company for supervision by the Board of Governors of the U.S. Federal Reserve System (the Board). The Council may designate by a two-thirds vote whether certain nonbank financial companies, including certain insurance companies and insurance holding companies, could pose a threat to the financial stability of the United States, in which case such nonbank financial companies would become subject to prudential regulation by the Board. On April 3, 2013, the Board published a final rule that establishes the requirements for determining when a nonbank financial company is "predominantly engaged in financial activities" - a prerequisite for designation by the Council. Prudential regulation by the Board includes supervision of capital requirements, leverage limits, liquidity requirements and examinations. The Board may limit such company's ability to enter into mergers, acquisitions and other business combination transactions, restrict its ability to offer financial products, require it to terminate one or more activities, or impose conditions on the manner in which it conducts activities. The Council designated two insurers in 2013 as a Systemically Important Financial Institution (SIFI). On March 30, 2016, the U.S. District Court for the District of Columbia reversed the SIFI designation of one of those insurers. The Council is currently appealing that decision. On December 18, 2014, the president signed the Insurance Capital Standards Clarification Act into law. This legislation will clarify the Board's authority to apply insurance-based capital standards for insurance companies subject to federal supervision. Although Aflac is a nonbank financial company predominantly engaged in financial activities as defined in the Dodd-Frank Act, we do not believe Aflac will be considered a company that poses a threat to the financial stability of the United States.

Title VII of the Dodd-Frank Act and regulations issued thereunder may have an impact on Aflac's derivative activity, including activity on behalf of Aflac Japan, in particular rules to require central clearing and collateral for certain types of derivatives. In 2015, six U.S. financial regulators, including the U.S. Commodity Futures Trading Commission (CFTC), issued final rules regarding uncleared swaps. Such rules become effective for Aflac on March 1, 2017 and may result in increased collateral requirements or affect other aspects of Aflac's derivatives activity.

The Dodd-Frank Act also established a Federal Insurance Office (FIO) under the U.S. Treasury Department to monitor all aspects of the insurance industry and of lines of business other than certain health insurance, certain long-term care insurance and crop insurance. Traditionally, U.S. insurance companies have been regulated primarily by state insurance departments. In December 2013, the FIO released a report entitled "How To Modernize And Improve The System Of Insurance Regulation In The United States." The report was required by the Dodd-Frank Act, and included 18 recommended areas of near-term reform for the states, including addressing capital adequacy and safety/soundness issues, reform of insurer resolution practices, and reform of marketplace regulation. The report also listed nine recommended areas for direct federal involvement in insurance regulation. Some of the recommendations outlined in the FIO report released in December 2013 have been implemented. Of the nine recommended areas for direct federal involvement in insurance regulation that are applicable to Aflac, the president signed the National

Association of Registered Agents and Brokers Reform Act into law in January 2015, which simplifies the agent and broker licensing process across state lines. The FIO has also engaged with the supervisory colleges to monitor financial stability and identify regulatory gaps for large national and internationally active insurers.

The process of implementing the Dodd-Frank Act is ongoing and continues to involve additional rulemaking from time to time. At the current time, it is not possible to predict with any degree of certainty what impact, if any, the Dodd-Frank Act will have on our U.S. business, financial condition, or results of operations.

Under state insurance guaranty association laws and similar laws in international jurisdictions, we are subject to assessments, based on the share of business we write in the relevant jurisdiction, for certain obligations of insolvent

insurance companies to policyholders and claimants. In the United States, some states permit member insurers to recover assessments paid through full or partial premium tax offsets. The Company's policy is to accrue assessments when the entity for which the insolvency relates has met its state of domicile's statutory definition of insolvency, the amount of the loss is reasonably estimable and the related premium upon which the assessment is based is written. In most states, the definition is met with a declaration of financial insolvency by a court of competent jurisdiction.

Penn Treaty Network Company and its subsidiary American Network Insurance Company (collectively referred to as Penn Treaty) were placed in rehabilitation on January 6, 2009, and remain in rehabilitation as of June 30, 2016. As of June 30, 2016, we were unable to estimate when or to what extent Penn Treaty will ultimately be declared insolvent, or the amount of the insolvency. As such, we have not established any accruals for guaranty fund assessments associated with Penn Treaty as of June 30, 2016.

#### Aflac U.S. Investments

The level of investment income is affected by available cash flow from operations, the timing of investing the cash flow, yields on new investments, and other factors.

Historically, Aflac U.S. has invested primarily in investment grade corporate bonds. In 2015, as part of our portfolio management and asset allocation process, Aflac U.S. purchased high yield corporate bonds and middle market loan receivables and initiated a commercial mortgage loan investment program. In the first six months of 2016, Aflac U.S. invested \$18 million in high yield corporate bonds; \$144 million in middle market loan receivables, of which \$31 million was unfunded; and \$23 million in commercial mortgage loans. As of June 30, 2016, we had commitments of \$72 million to fund potential future loan originations related to the middle market loan investment program. These commitments are contingent upon the availability of middle market loans that meet our underwriting criteria. See Note 3 of the Notes to the Consolidated Financial Statements and Notes 1 and 3 of Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015 for more information regarding loans and loans receivables.

Starting in the first quarter of 2016, we initiated an allocation to dividend focused U.S. public equities. These equities had a cost basis of \$91 million as of June 30, 2016.

The following table presents the results of Aflac's U.S. investment yields for the periods ended June 30.

|  | Three Months |        | Six Months |        |
|--|--------------|--------|------------|--------|
|  | 2016         | 2015   | 2016       | 2015   |
| New money yield <sup>(1)</sup>   | 3.70 %       | 4.56 % | 4.16 %     | 4.17 % |
| Return on average invested assets, net of investment expenses <sup>(2)</sup> | 5.04         | 5.26   | 5.03       | 5.24   |
| Portfolio book yield, end of period <sup>(1)</sup>                           | 5.69 %       | 5.82 % | 5.69 %     | 5.82 % |

<sup>(1)</sup> Includes fixed maturities and perpetual securities, loan receivables, and equities

<sup>(2)</sup> Net of investment expenses, year-to-date number reflected on a quarterly average basis

The decrease in the Aflac U.S. new money yield for the three- and six-month periods ended June 30, 2016 was primarily due to a general decline in U.S. interest rates. See Notes 3 and 5 of the Notes to the Consolidated Financial Statements and the Analysis of Financial Condition section of this MD&A for additional information on our investments.

#### ANALYSIS OF FINANCIAL CONDITION

Our financial condition has remained strong in the functional currencies of our operations. The yen/dollar exchange rate at the end of each period is used to translate yen-denominated balance sheet items to U.S. dollars for reporting purposes.

The following table demonstrates the effect of the change in the yen/dollar exchange rate by comparing select balance sheet items as reported at June 30, 2016, with the amounts that would have been reported had the exchange rate remained unchanged from December 31, 2015.

## Impact of Foreign Exchange on Balance Sheet Items

| (In millions)                           | As Reported | Exchange Effect | Net of Exchange Effect <sup>(1)</sup> |
|---|-------------|-----------------|---------------------------------------|
| Yen/dollar exchange rate <sup>(2)</sup> | 102.91      |                 | 120.61                                |
| Investments and cash                    | \$ 125,983  | \$ 12,040       | \$ 113,943                            |
| Deferred policy acquisition costs       | 9,552       | 938             | 8,614                                 |
| Policy liabilities                      | 103,066     | 13,652          | 89,414                                |

<sup>(1)</sup>Amounts excluding foreign currency changes on dollar-denominated items (a non-U.S. GAAP measure) were determined using the same yen/dollar exchange rate for the current period as the comparable period in the prior year.

<sup>(2)</sup>The exchange rate at June 30, 2016, was 102.91 yen to one dollar, or 17.2% stronger than the December 31, 2015, exchange rate of 120.61.

## Market Risks of Financial Instruments

Our investment philosophy is to fulfill our fiduciary responsibility to invest assets in a prudent manner to meet the present and future needs of our policyholders' contractual obligations while maximizing the long-term financial return on assets consistent with the company goal of maximizing long-term shareholder value within defined risk appetites, limits, and maintaining adequate liquidity.

The following table details investment securities by segment.

Investment Securities by Segment <sup>(1)</sup>

| (In millions)                                   | Aflac Japan   |                   | Aflac U.S.    |                   |
|---|---------------|-------------------|---------------|-------------------|
|   | June 30, 2016 | December 31, 2015 | June 30, 2016 | December 31, 2015 |
| Securities available for sale, at fair value:   |               |                   |               |                   |
| Fixed maturities                                | \$ 65,946     | \$ 52,304         | \$ 13,742     | \$ 12,522         |
| Perpetual securities                            | 1,780         | 1,890             | 52            | 57                |
| Equity securities                               | 1,096         | 493               | 101           | 5                 |
| Total available for sale                        | 68,822        | 54,687            | 13,895        | 12,584            |
| Securities held to maturity, at amortized cost: |               |                   |               |                   |
| Fixed maturities                                | 38,346        | 33,459            | 0             | 0                 |
| Total held to maturity                          | 38,346        | 33,459            | 0             | 0                 |
| Total investment securities                     | \$ 107,168    | \$ 88,146         | \$ 13,895     | \$ 12,584         |

<sup>(1)</sup>Excludes available-for-sale fixed-maturity securities held by the Parent Company and other business segments of \$598 in 2016 and \$523 in 2015.

Because we invest primarily in fixed-maturity securities, our financial instruments are exposed primarily to three types of market risks: currency risk, interest rate risk, and credit risk. In 2015 and continuing into the first six months of 2016, we increased our investment allocation to dividend focused yen-denominated and U.S. dollar-denominated public equity securities, thereby increasing our exposure to equity risk.

## Currency Risk

The functional currency of Aflac Japan's insurance operations is the Japanese yen. All of Aflac Japan's premiums, claims and commissions are received or paid in yen, as are most of its other expenses. Most of Aflac Japan's cash and liabilities are yen-denominated. Aflac Japan's investments consisted of yen-denominated fixed income securities of \$72.7 billion, at amortized cost, and yen-denominated equity securities of \$694 million, at cost, at June 30, 2016. However, Aflac Japan also owns U.S. dollar-denominated fixed income securities of \$15.4 billion, at amortized cost, whose fair value is hedged against currency risk as well as \$9.6 billion of fixed income securities, at cost, that are not hedged as of June 30, 2016. Aflac Japan owns U.S. dollar-denominated equity securities of \$457 million, at cost, that

are not hedged as of June 30, 2016. Yen-denominated investment income accounted for 53% and 52% of Aflac Japan's investment income during the three- and six-month periods ended June 30, 2016, respectively, with the remainder denominated in U.S. dollars. In addition, Aflac Incorporated has yen-denominated debt obligations.



Subsequent to the end of the second quarter, in July 2016 Aflac Japan hedged more of these U.S. dollar-denominated asset classes against currency risk, including \$1.9 billion of senior secured bank loans that are included in the U.S. dollar-denominated fixed income securities category above and \$457 million of U.S. dollar-denominated equity securities. We continually evaluate our hedging strategy.

We are exposed to currency risk as an economic event only when yen funds are actually converted into dollars. This occurs when we repatriate yen-denominated funds from Aflac Japan to Aflac U.S and with quarterly settlements of our reinsurance retrocession transactions. The exchange rates prevailing at the time of profit repatriation will differ from the exchange rates prevailing at the time the yen profits were earned. A portion of the yen repatriation may be used to service Aflac Incorporated's yen-denominated notes payable with the remainder converted into dollars. In order to economically hedge foreign exchange risk for a portion of the profit repatriation received in yen from Aflac Japan, we had foreign exchange forwards and options as part of a hedging strategy on 25.0 billion yen received in February 2016. As of June 30, 2016, we had foreign exchange forwards and options to economically hedge foreign exchange risk on 51.1 billion yen of profit repatriation received in July 2016 and 109.0 billion yen of future profit repatriation from Aflac Japan.

In addition to profit repatriation and the reinsurance retrocessions, certain investment activities for Aflac Japan expose us to economic currency risk when yen are converted into dollars. As noted above, we invest a portion of our yen cash flows in U.S. dollar-denominated assets. This requires that we convert the yen cash flows to U.S. dollars before investing. As previously discussed, for certain of our U.S. dollar-denominated securities, we enter into foreign currency forward and option contracts to hedge the currency risk on the fair value of the securities. The dollar coupon payments received on these investments are not hedged and are subject to foreign exchange fluctuations, which are realized in earnings. Also, Aflac Japan has invested in reverse-dual currency securities (RDCs, or yen-denominated debt securities with dollar coupon payments), which exposes Aflac to changes in foreign exchange rates. The foreign currency effect on the yen-denominated securities is accounted for as a component of unrealized gains or losses on available-for-sale securities in accumulated other comprehensive income, while the foreign currency effect on the dollar coupons is realized in earnings. The RDCs provided a higher yield at the time of purchase than those available on Japanese government or other public corporate bonds, while still adhering to our investment standards at the time of the transaction. The yen/dollar exchange rate would have to strengthen significantly before the yield on these instruments would equal that of a comparable JGB instrument.

Aside from the activities discussed above, we generally do not convert yen into dollars; however, we do translate financial statement amounts from yen into dollars for financial reporting purposes. Therefore, reported amounts are affected by foreign currency fluctuations. We report unrealized foreign currency translation gains and losses in accumulated other comprehensive income. In periods when the yen weakens against the dollar, translating yen into dollars causes fewer dollars to be reported. When the yen strengthens, translating yen into dollars causes more dollars to be reported. The weakening of the yen relative to the dollar will generally adversely affect the value of our yen-denominated investments in dollar terms. We attempt to minimize the exposure of shareholders' equity to foreign currency. We accomplish this by investing a portion of Aflac Japan's investment portfolio in U.S. dollar-denominated securities and by the Parent Company's issuance of yen-denominated debt (for additional information, see the discussion under the Hedging Activities subsection of MD&A). As a result, the effect of currency fluctuations on our net assets is reduced.

The following table demonstrates the effect of foreign currency fluctuations by presenting the dollar values of our yen-denominated assets and liabilities, and our consolidated yen-denominated net asset exposure at selected exchange rates.

Dollar Value of Yen-Denominated Assets and Liabilities  
at Selected Exchange Rates

| (In millions)  | June 30, 2016 |                       |           | December 31, 2015 |                       |            |
|--|---------------|-----------------------|-----------|-------------------|-----------------------|------------|
| Yen/dollar exchange rates  | 87.91         | 102.91 <sup>(1)</sup> | 117.91    | 105.61            | 120.61 <sup>(1)</sup> | 135.61     |
| Yen-denominated financial instruments:   |               |                       |           |                   |                       |            |
| Assets:  |               |                       |           |                   |                       |            |
| Securities available for sale:   |               |                       |           |                   |                       |            |
| Fixed maturities <sup>(2)</sup>  | \$45,188      | \$38,601              | \$33,690  | \$31,544          | \$27,621              | \$24,566   |
| Fixed maturities - consolidated variable interest entities <sup>(3)</sup>                                    | 1,277         | 1,091                 | 952       | 1,016             | 890                   | 792        |
| Perpetual securities   | 1,839         | 1,571                 | 1,371     | 1,883             | 1,649                 | 1,466      |
| Perpetual securities - consolidated variable interest entities <sup>(3)</sup>                                | 224           | 191                   | 167       | 214               | 187                   | 167        |
| Equity securities  | 174           | 149                   | 130       | 408               | 357                   | 318        |
| Equity securities - consolidated variable interest entities  | 583           | 498                   | 435       | 149               | 130                   | 116        |
| Securities held to maturity:   |               |                       |           |                   |                       |            |
| Fixed maturities   | 44,889        | 38,346                | 33,468    | 38,212            | 33,459                | 29,758     |
| Cash and cash equivalents  | 1,642         | 1,403                 | 1,224     | 730               | 640                   | 569        |
| Derivatives  | 4,667         | 1,963                 | 702       | 2,416             | 676                   | 968        |
| Other financial instruments  | 226           | 193                   | 169       | 179               | 156                   | 139        |
| Subtotal   | 100,709       | 84,006                | 72,308    | 76,751            | 65,765                | 58,859     |
| Liabilities:   |               |                       |           |                   |                       |            |
| Notes payable  | 281           | 241                   | 210       | 234               | 205                   | 183        |
| Derivatives  | 1,173         | 542                   | 863       | 545               | 371                   | 1,901      |
| Subtotal   | 1,454         | 783                   | 1,073     | 779               | 576                   | 2,084      |
| Net yen-denominated financial instruments  | 99,255        | 83,223                | 71,235    | 75,972            | 65,189                | 56,775     |
| Other yen-denominated assets   | 9,913         | 8,468                 | 7,391     | 8,195             | 7,176                 | 6,382      |
| Other yen-denominated liabilities  | 117,279       | 100,185               | 87,440    | 94,775            | 82,988                | 73,808     |
| Consolidated yen-denominated net assets (liabilities) subject to foreign currency fluctuation <sup>(2)</sup> | \$(8,111)     | \$(8,494)             | \$(8,814) | \$(10,608)        | \$(10,623)            | \$(10,651) |

<sup>(1)</sup> Actual period-end exchange rate

<sup>(2)</sup> Does not include the U.S. dollar-denominated corporate bonds for which we have entered into foreign currency derivatives as discussed in the Aflac Japan Investment subsection of MD&A

<sup>(3)</sup> Does not include U.S. dollar-denominated bonds that have corresponding cross-currency swaps in consolidated VIEs

We are required to consolidate certain VIEs. Some of the consolidated VIEs in Aflac Japan's portfolio use foreign currency swaps to convert foreign denominated cash flows to yen, the functional currency of Aflac Japan, in order to minimize cash flow fluctuations. Foreign currency swaps exchange an initial principal amount in two currencies, agreeing to re-exchange the currencies at a future date, at an agreed upon exchange rate. There may also be periodic exchanges of payments at specified intervals based on the agreed upon rates and notional amounts. Prior to consolidation, our beneficial interest in these VIEs was a yen-denominated available-for-sale fixed maturity security. Upon consolidation, the original yen-denominated investment was derecognized and the underlying fixed-maturity or perpetual securities and cross-currency swaps were recognized. The combination of a U.S. dollar-denominated investment and cross-currency swap economically creates a yen-denominated investment and has no impact on our net investment hedge position.

Similarly, the combination of the U.S. corporate bonds and the foreign currency forwards and options that we have entered into, as discussed in the Aflac Japan Investment subsection of MD&A, economically creates a yen-denominated investment that qualifies for inclusion as a component of our investment in Aflac Japan for net investment hedge purposes.

For additional information regarding our Aflac Japan net investment hedge, see the Hedging Activities subsection of MD&A.

#### Interest Rate Risk

Our primary interest rate exposure is to the impact of changes in interest rates on the fair value of our investments in debt and perpetual securities. We estimate that the reduction in the fair value of debt and perpetual securities we own resulting from a 100 basis point increase in Japan and U.S. interest rates, based on our portfolios at June 30, 2016, and December 31, 2015, would be as follows:

| (In millions)  | June 30,<br>2016 | December 31,<br>2015 |
|--|------------------|----------------------|
| Effect on yen-denominated debt and perpetual securities    | \$(12,367)       | \$(8,693 )           |
| Effect on dollar-denominated debt and perpetual securities | (3,439 )         | (4,482 )             |
| Effect on total debt and perpetual securities              | \$(15,806)       | \$(13,175 )          |

There are various factors that affect the fair value of our investment in debt and perpetual securities. Included in those factors are changes in the prevailing interest rate environment, which directly affect the balance of unrealized gains or losses for a given period in relation to a prior period. Decreases in market yields generally improve the fair value of debt and perpetual securities, while increases in market yields generally have a negative impact on the fair value of our debt and perpetual securities. However, we do not expect to realize a majority of any unrealized gains or losses because we generally have the intent and ability to hold such securities until a recovery of value, which may be maturity. For additional information on unrealized losses on debt and perpetual securities, see Note 3 of the Notes to the Consolidated Financial Statements.

We perform extensive analysis on the duration of our assets and liabilities. Currently, when debt and perpetual securities we own mature, the proceeds may be reinvested at a yield below that of the interest required for the accretion of policy benefit liabilities on policies issued in earlier years. However, adding riders to our older policies has helped offset negative investment spreads on these policies. Overall, adequate profit margins exist in Aflac Japan's aggregate block of business because of changes in the mix of business and favorable experience from mortality, morbidity and expenses.

Periodically, depending on general economic conditions, we may enter into other derivative transactions to hedge interest rate risk.

For further information on our interest rate derivatives, see Note 4 of the Notes to the Consolidated Financial Statements and the Interest Rate Risk subsection of MD&A in our annual report to shareholders for the year ended December 31, 2015.

#### Credit Risk

A significant portion of our investment portfolio consists of debt securities or perpetual securities that expose us to the credit risk of the underlying issuer. We carefully evaluate this risk on every new investment and closely monitor the credit risk of our existing investment portfolio. We incorporate the needs of our products and liabilities, the overall requirements of the business, and other factors in addition to our underwriting of the credit risk for each investment in the portfolio.

Evaluating the underlying risks in our credit portfolio involves a multitude of factors including but not limited to our assessment of the issuers business activities, assets, products, market position, financial condition, and future prospects. We also must incorporate the assessment of the Nationally Recognized Statistical Rating Organizations (NRSROs) in assigning credit ratings to our specific portfolio holdings. We perform extensive internal assessments of the credit risks for all our portfolio holdings and potential new investments.

The ratings of our securities referenced in the two tables below are based on the ratings designations provided by major NRSROs (Moody's, S&P and Fitch) or, if not rated, are determined based on our internal analysis of such securities. For investment-grade securities where the ratings assigned by the major credit agencies are not equivalent,

we use the second lowest rating that is assigned. For a description of the ratings methodology that we use when a security is below investment grade or split-rated, see "Market Risks of Financial Instruments - Below-Investment-Grade and Split-Rated Securities" in the Analysis of Financial Condition section of this MD&A.

The distributions by credit rating of our purchases of debt securities, based on acquisition cost, were as follows:

Composition of Purchases by Credit Rating

|             | Six<br>Months<br>Ended<br>June 30,<br>2016 | Twelve<br>Months<br>Ended<br>December<br>31, 2015 | Six<br>Months<br>Ended<br>June 30,<br>2015 |
|-------------|--|---|--|
| AAA         | 13.7 %                                     | 1.4 %   | 2.4 %                                      |
| AA          | 1.6  | 1.6   | 2.9  |
| A           | 48.3                                       | 39.3  | 14.8                                       |
| BBB         | 18.1                                       | 25.7  | 30.8                                       |
| BB or lower | 18.3                                       | 32.0  | 49.1                                       |
| Total       | 100.0%                                     | 100.0 %   | 100.0%                                     |

Purchases of securities from period to period are determined based on multiple objectives including appropriate portfolio diversification, the relative value of a potential investment and availability of investment opportunities, liquidity, credit and other risk factors while adhering to our investment policy guidelines. We did not purchase any perpetual securities during the periods presented in the table above. Total purchases comprise new money investments as well as the reinvestment of proceeds from investment disposals. In the first six months of 2016, the increase in purchases of AAA rated securities was due primarily to the purchase of high quality yen bonds. In the first six months of 2016, the increase in purchases of A rated securities was due primarily to the purchase of JGBs. In the full year of 2015, purchases of A rated and BBB rated securities were driven primarily by the purchase of U.S.

dollar-denominated corporate fixed-income publicly traded securities for the Aflac Japan portfolio. In the full year of 2015, the purchases of BB or lower rated securities were driven by an increased investment in senior secured bank loans, most of which have below-investment-grade ratings, and investment in high yield corporate bonds. The bank loan investment program is managed externally by third party firms specializing in this asset class. This mandate requires a minimum average credit quality of BB-/Ba3, prohibits loan purchases rated below B/B2, and restricts exposure to any individual credit to less than 2% of the program's assets. The objectives of this program include enhancing the yield on invested assets, achieving further diversification of credit risk, and mitigating the risk of rising interest rates through the acquisition of floating rate assets. The objective of the high yield corporate bond investments is to enhance yield on invested assets and further diversify our credit risk. All high yield corporate bond investments must have a minimum rating of low BB using our above described rating methodology and are managed by our internal credit portfolio management team.

The distributions of debt and perpetual securities we own, by credit rating, were as follows:

Composition of Portfolio by Credit Rating

|             | June 30, 2016     |               | December 31, 2015 |               |
|-------------|-------------------|---------------|-------------------|---------------|
|             | Amortized<br>Cost | Fair<br>Value | Amortized<br>Cost | Fair<br>Value |
| AAA         | 1.7 %             | 1.5 %         | 1.3 %             | 1.3 %         |
| AA          | 5.1               | 4.9           | 5.7               | 5.7           |
| A           | 61.9              | 66.1          | 61.0              | 63.0          |
| BBB         | 26.0              | 23.2          | 26.9              | 25.1          |
| BB or lower | 5.3               | 4.3           | 5.1               | 4.9           |
| Total       | 100.0 %           | 100.0 %       | 100.0 %           | 100.0 %       |

As of June 30, 2016, our direct and indirect exposure to securities in our investment portfolio that were guaranteed by third parties was immaterial both individually and in the aggregate.

Portfolio Composition

For information regarding the amortized cost for our investments in debt and perpetual securities, the cost for equity securities and the fair values of these investments, refer to Note 3 of the Notes to the Consolidated Financial Statements.



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Investment Concentrations

Our 15 largest global debt and perpetual investment exposures as of June 30, 2016, were as follows:

Largest Global Investment Positions

| (In millions)  | Amortized Cost | % of Total | Seniority     | Ratings |      |       |
|--|----------------|------------|---------------|---------|------|-------|
|  |                |            |               | Moody's | S&P  | Fitch |
| Japan National Government <sup>(1)</sup>                     | \$45,064       | 40.87 %    | Senior        | A1      | A+   | A     |
| Japan Housing Finance Agency                                 | 686            | .62        |               |         |      |       |
| Japan Housing Finance Agency                                 | 597            | .54        | Senior        | —       | AAA  | —     |
| Government Housing Loan Co.                                  | 68             | .06        | Senior        | —       | AAA  | —     |
| MR Trust Class B   | 21             | .02        | Senior        | A1      | —    | —     |
| Republic of South Africa                                     | 583            | .53        | Senior        | Baa2    | BBB- | BBB-  |
| Bank of America NA   | 439            | .40        |               |         |      |       |
| Bank of America Corp.  | 243            | .22        | Senior        | Baa1    | BBB+ | A     |
| Bank of America Corp.  | 194            | .18        | Lower Tier II | Baa3    | BBB  | A-    |
| Bank of America NA   | 2              | .00        | Senior        | A1      | A    | A+    |
| Bank of Tokyo-Mitsubishi UFJ Ltd.                            | 437            | .40        |               |         |      |       |
| BTMU Curacao Holdings NV                                     | 437            | .40        | Lower Tier II | A2      | —    | A-    |
| Investcorp SA  | 409            | .37        |               |         |      |       |
| Investcorp Capital Limited                                   | 359            | .32        | Senior        | Ba2     | —    | BB    |
| Investcorp Capital Limited                                   | 50             | .05        | Senior        | Ba2     | —    | —     |
| JP Morgan Chase & Co.  | 377            | .34        |               |         |      |       |
| JPMorgan Chase & Co. (including Bear Stearns Companies Inc.) | 342            | .30        | Senior        | A3      | A-   | A+    |
| JPMorgan Chase & Co. (Bank One Corp.)                        | 17             | .02        | Lower Tier II | Baa1    | BBB+ | A     |
| JPMorgan Chase & Co. (NBD Bank)                              | 11             | .01        | Lower Tier II | A1      | A-   | A     |
| JPMorgan Chase & Co. (FNBC)                                  | 7              | .01        | Senior        | Aa1     | A+   | —     |
| Banobras   | 360            | .33        | Senior        | A3      | BBB+ | BBB+  |
| Sultanate of Oman  | 340            | .31        | Senior        | Baa1    | BBB- | —     |
| Koninklijke Ahold NV   | 335            | .30        |               |         |      |       |
| Koninklijke Ahold NV   | 321            | .29        | Senior        | Baa2    | BBB  | BBB   |
| Ahold USA Lease  | 14             | .01        | Senior        | Baa2    | BBB  | —     |
| Nordea Bank AB   | 327            | .30        |               |         |      |       |
| Nordea Bank AB   | 250            | .23        | Tier I        | Baa3    | BBB  | —     |
| Nordea Bank Finland  | 77             | .07        | Upper Tier II | Baa2    | —    | —     |
| Petroleos Mexicanos (Pemex)                                  | 323            | .29        |               |         |      |       |
| Pemex Proj FDG Master TR                                     | 291            | .26        | Senior        | Baa3    | BBB+ | BBB+  |
| Pemex Finance Ltd.   | 32             | .03        | Senior        | Baa3    | A    | A+    |
| AXA  | 313            | .28        |               |         |      |       |
| AXA-UAP  | 262            | .23        | Upper Tier II | A3      | BBB  | BBB   |
| AXA  | 51             | .05        | CC FNB        | A3      | BBB  | BBB+  |
| Deutsche Telekom AG  | 313            | .28        |               |         |      |       |
| Deutsche Telekom AG  | 292            | .26        | Senior        | Baa1    | BBB+ | BBB+  |
| Deutsche Telekom International Finance                       | 21             | .02        | Senior        | Baa1    | BBB+ | BBB+  |
| CFE  | 311            | .28        | Senior        | Baa1    | BBB+ | BBB+  |



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|  |            |         |
|--|------------|---------|
| Subtotal   | \$ 50,617  | 45.90 % |
| Total debt and perpetual securities<br>(1) JGBs or JGB-backed securities | \$ 110,261 | 100.00% |

As previously disclosed, we own long-dated debt instruments in support of our long-dated policyholder obligations. Some of our largest global investment holdings are positions that were purchased many years ago and increased in size due to merger and consolidation activity among the issuing entities. In addition, many of our largest holdings are yen-denominated, therefore strengthening of the yen can increase our position in dollars, and weakening of the yen can decrease our position in dollars. Our global investment guidelines establish concentration limits for our investment portfolios.

## Geographical Exposure

The following table indicates the geographic exposure of our debt and perpetual investment portfolio.

| (In millions)                           | June 30, 2016  |            | December 31, 2015 |            |
|---|----------------|------------|-------------------|------------|
|   | Amortized Cost | % of Total | Amortized Cost    | % of Total |
| Japan                                   | \$48,878       | 44.3 %     | \$39,593          | 41.3 %     |
| United States and Canada <sup>(1)</sup> | 34,167         | 31.0       | 31,622            | 33.0       |
| United Kingdom                          | 2,650          | 2.4        | 2,697             | 2.8        |
| Germany                                 | 2,975          | 2.7        | 2,558             | 2.7        |
| France                                  | 1,998          | 1.8        | 1,755             | 1.8        |
| Peripheral Eurozone                     | 2,926          | 2.6        | 2,762             | 2.9        |
| Portugal                                | 228            | .2         | 200               | .2         |
| Italy                                   | 1,774          | 1.6        | 1,514             | 1.6        |
| Ireland                                 | 130            | .1         | 364               | .4         |
| Spain                                   | 794            | .7         | 684               | .7         |
| Nordic Region                           | 2,044          | 1.9        | 1,906             | 1.9        |
| Sweden                                  | 794            | .7         | 682               | .7         |
| Norway                                  | 584            | .5         | 512               | .5         |
| Denmark                                 | 292            | .3         | 332               | .3         |
| Finland                                 | 374            | .4         | 380               | .4         |
| Other Europe                            | 2,905          | 2.7        | 2,502             | 2.6        |
| Netherlands                             | 1,597          | 1.5        | 1,367             | 1.4        |
| Switzerland                             | 274            | .3         | 246               | .3         |
| Czech Republic                          | 486            | .4         | 415               | .4         |
| Austria                                 | 135            | .1         | 115               | .1         |
| Belgium                                 | 212            | .2         | 182               | .2         |
| Poland                                  | 194            | .2         | 166               | .2         |
| Luxembourg                              | 7              | .0         | 11                | .0         |
| Asia excluding Japan                    | 3,826          | 3.5        | 3,325             | 3.5        |
| Africa and Middle East                  | 2,839          | 2.6        | 2,478             | 2.6        |
| Latin America                           | 2,430          | 2.2        | 2,172             | 2.3        |
| Australia                               | 2,122          | 1.9        | 2,135             | 2.2        |
| All Others                              | 501            | .4         | 437               | .4         |
| Total debt and perpetual securities     | \$110,261      | 100.0%     | \$95,942          | 100.0%     |

<sup>(1)</sup> Includes total exposure to Puerto Rico of \$1 million of required deposits for both June 30, 2016 and December 31, 2015, of which

100% and 72% had principal and interest insurance as of June 30, 2016 and December 31, 2015, respectively.

The primary factor considered when determining the domicile of investment exposure is the legal country risk location of the issuer. However, other factors such as the location of the parent guarantor, the location of the company's headquarters or major business operations (including location of major assets), location of primary market (including location of revenue generation) and specific country risk publicly recognized by rating agencies can influence the assignment of the country (or geographic) risk location. When the issuer is a special financing vehicle or a branch or subsidiary of a global company, then we consider any guarantees and/or legal, regulatory and corporate relationships of the issuer relative to its ultimate parent in determining the proper assignment of country risk.

## European sovereign debt crisis

Beginning in 2008, many countries in Europe, and specifically Greece, Ireland, Italy, Portugal, and Spain, experienced a debt crisis. Collective action by multiple parties including the European Central Bank (ECB), International Monetary Fund (IMF), European Council, and individual member states' governments have helped stabilize the situation across



Europe. In exchange for this support, affected countries generally agreed to implement a series of measures to improve their fiscal situation in exchange for loans and other aid. Most countries continue to implement the prescribed austerity measures and have seen improvement in their economies, which in turn has seen their creditworthiness improve or stabilize.

Although recent economic indicators show improvement from the depths of the crisis across most of the Eurozone, overall economic activity remains subdued throughout the region. To support the return to sustainable economic growth, the ECB has launched a quantitative easing (QE) stimulus program. Throughout the crisis period, we took steps to improve the risk profile of our European holdings.

The recent referendum in the United Kingdom (UK) to leave the European Union (EU) has added a new level of uncertainty to Europe's economic recovery. The ultimate outcome of the "Brexit" vote on UK and EU political and economic stability is uncertain but the near term result was a spike in market volatility. Although markets have since stabilized, many questions remain regarding the ultimate impact to the UK and other EU countries' economies, as well as potential policy action which may be taken by the UK government, the Bank of England, the EU, and the ECB.

**Investments in Certain European Countries - monitoring and mitigating exposure**

Our internal team of experienced credit professionals closely monitors the credit quality of our individual investment holdings. Our analysis includes factors beyond a baseline assessment of a company's assets, operations, financial statements, and credit metrics that may provide support for the instruments we own. Specifically, for our investments in Europe, this analysis includes items such as the importance of the issuer to a local market's economy, the likelihood of government support, our investment's position in the capital structure, and the value of the underlying assets.

Additionally, some of our European fixed-maturity investments contain covenants that we believe mitigate our risk to the issuer. These covenants could include put options that allow us to return our holdings to the issuer at a predetermined price, usually par, should the issuer be downgraded to below investment grade by a rating agency.

Additionally, these covenants may include restrictions on the ability of the issuer to incur additional debt, sell assets, or provide collateral for indebtedness. As of June 30, 2016, all of the issuers of our holdings from European issuers were current on their obligations to us, and we believe they have the ability to meet their obligations to us.

Although the situation has largely stabilized across Europe, we note the increased uncertainty as a result of the Brexit vote in the UK. We continue to monitor the entirety of the European situation closely including the heightened interrelationship between political, monetary, fiscal, and economic forces; the pace of underlying structural reforms; the possibility of continued contagion to additional sovereigns and other entities; further stress on the banking systems throughout the region; and the impact on the underlying economic fundamentals throughout the Eurozone.

**Oil and Gas Exposure**

As a result of the significant decline in oil prices, which began in the fourth quarter of 2014 and continued through most of 2015, there has been heightened attention to certain investments in the various energy sub-sectors related to the oil and gas industry. Our portfolio includes holdings diversified across multiple sub-sectors of the oil and gas industry, spread among multiple geographies. The following tables show the breakout of our exposure to the oil and gas industry.

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| (In millions)   | June 30, 2016          |                        |                         | Fair Value |
|---|------------------------|------------------------|-------------------------|------------|
|   | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses |            |
| Securities available for sale,<br>carried at fair value:    |                        |                        |                         |            |
| Fixed maturities:   |                        |                        |                         |            |
| Independent exploration and production                      | \$1,331                | \$ 76                  | \$ 61                   | \$1,346    |
| Integrated energy   | 640                    | 58                     | 35                      | 663        |
| Midstream   | 1,293                  | 101                    | 56                      | 1,338      |
| Oil field services  | 1,103                  | 27                     | 206                     | 924        |
| Refiners  | 471                    | 14                     | 11                      | 474        |
| Government owned - energy related                           | 974                    | 186                    | 18                      | 1,142      |
| Natural gas utilities                                       | 374                    | 79                     | 1                       | 452        |
| Total fixed maturities                                      | 6,186                  | 541                    | 388                     | 6,339      |
| Equity securities:  |                        |                        |                         |            |
| Integrated energy   | 21                     | 1                      | 0                       | 22         |
| Midstream   | 8                      | 2                      | 0                       | 10         |
| Refiners  | 6                      | 0                      | 1                       | 5          |
| Total equity securities                                     | 35                     | 3                      | 1                       | 37         |
| Total securities available for sale                         | 6,221                  | 544                    | 389                     | 6,376      |
| Securities held to maturity,<br>carried at amortized cost:  |                        |                        |                         |            |
| Fixed maturities:   |                        |                        |                         |            |
| Integrated energy   | 253                    | 19                     | 0                       | 272        |
| Government owned - energy related                           | 292                    | 8                      | 0                       | 300        |
| Natural gas utilities                                       | 243                    | 39                     | 0                       | 282        |
| Total fixed maturities                                      | 788                    | 66                     | 0                       | 854        |
| Total securities held to maturity                           | 788                    | 66                     | 0                       | 854        |
| Total securities available for sale<br>and held to maturity | \$7,009                | \$ 610                 | \$ 389                  | \$7,230    |

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| (In millions)   | December 31, 2015      |                        |                         | Fair Value |
|---|------------------------|------------------------|-------------------------|------------|
|   | Cost or Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses |            |
| Securities available for sale,<br>carried at fair value:    |                        |                        |                         |            |
| Fixed maturities:   |                        |                        |                         |            |
| Independent exploration and production                      | \$1,270                | \$ 73                  | \$ 139                  | \$1,204    |
| Integrated energy   | 575                    | 55                     | 27                      | 603        |
| Midstream   | 1,246                  | 76                     | 144                     | 1,178      |
| Oil field services  | 1,155                  | 27                     | 228                     | 954        |
| Refiners  | 460                    | 6                      | 30                      | 436        |
| Government owned - energy related                           | 887                    | 182                    | 25                      | 1,044      |
| Natural gas utilities                                       | 344                    | 53                     | 1                       | 396        |
| Total fixed maturities                                      | 5,937                  | 472                    | 594                     | 5,815      |
| Equity securities   | 3                      | 0                      | 0                       | 3          |
| Total securities available for sale                         | 5,940                  | 472                    | 594                     | 5,818      |
| Securities held to maturity,<br>carried at amortized cost:  |                        |                        |                         |            |
| Fixed maturities:   |                        |                        |                         |            |
| Integrated energy   | 242                    | 9                      | 0                       | 251        |
| Government owned - energy related                           | 249                    | 5                      | 0                       | 254        |
| Natural gas utilities                                       | 207                    | 18                     | 0                       | 225        |
| Total fixed maturities                                      | 698                    | 32                     | 0                       | 730        |
| Total securities held to maturity                           | 698                    | 32                     | 0                       | 730        |
| Total securities available for sale<br>and held to maturity | \$6,638                | \$ 504                 | \$ 594                  | \$6,548    |

As of June 30, 2016, the weighted-average rating of our total fixed maturity energy exposure is BBB, and 88% of our exposure to the oil and gas industry is investment grade, compared to 93% at December 31, 2015. Absent a major change in the outlook for oil prices, we expect the increase in market volatility surrounding these issuers to continue. This could lead to additional negative ratings activity from the public rating agencies for energy credit issuers. We do not currently expect our investments in the energy sector to have a material impact on our results of operations.

#### Securities by Type of Issuance

We have investments in both publicly and privately issued securities. Our ability to sell either type of security is a function of overall market liquidity which is impacted by, among other things, the amount of outstanding securities of a particular issuer or issuance, trading history of the issue or issuer, overall market conditions, and idiosyncratic events affecting the specific issue or issuer.

The following table details investment securities by type of issuance.

#### Investment Securities by Type of Issuance

| (In millions)                               | June 30, 2016  |            | December 31, 2015 |            |
|---|----------------|------------|-------------------|------------|
|   | Amortized Cost | Fair Value | Amortized Cost    | Fair Value |
| Publicly issued securities:                 |                |            |                   |            |
| Fixed maturities                            | \$80,243       | \$97,363   | \$68,528          | \$74,933   |
| Perpetual securities                        | 52             | 69         | 77                | 111        |
| Equity securities                           | 1,237          | 1,188      | 473               | 489        |
| Total publicly issued                       | 81,532         | 98,620     | 69,078            | 75,533     |
| Privately issued securities: <sup>(1)</sup> |                |            |                   |            |
| Fixed maturities                            | 28,102         | 31,719     | 25,573            | 27,936     |
| Perpetual securities                        | 1,864          | 1,763      | 1,764             | 1,836      |
| Equity securities                           | 8              | 9          | 7                 | 9          |
| Total privately issued                      | 29,974         | 33,491     | 27,344            | 29,781     |
| Total investment securities                 | \$111,506      | \$132,111  | \$96,422          | \$105,314  |

<sup>(1)</sup> Includes Rule 144A securities

The following table details our privately issued investment securities.

#### Privately Issued Securities

| (Amortized cost, in millions)  | June 30, 2016 |   | December 31, 2015 |   |
|--|---------------|---|-------------------|---|
| Privately issued securities as a percentage of total investment securities                     | 26.9          | % | 28.4              | % |
| Privately issued securities held by Aflac Japan  | \$27,274      |   | \$24,602          |   |
| Privately issued securities held by Aflac Japan as a percentage of total investment securities | 24.5          | % | 25.5              | % |

#### Reverse-Dual Currency Securities<sup>(1)</sup>

| (Amortized cost, in millions)   | June 30, 2016 |   | December 31, 2015 |   |
|---|---------------|---|-------------------|---|
| Privately issued reverse-dual currency securities                               | \$6,371       |   | \$5,372           |   |
| Publicly issued collateral structured as reverse-dual currency securities       | 1,527         |   | 1,303             |   |
| Total reverse-dual currency securities  | \$7,898       |   | \$6,675           |   |
| Reverse-dual currency securities as a percentage of total investment securities | 7.1           | % | 6.9               | % |

<sup>(1)</sup> Principal payments in yen and interest payments in dollars

Aflac Japan has invested in privately issued securities to better match liability characteristics and secure higher yields than those available on Japanese government or other public corporate bonds. All of the yen-denominated privately issued securities we have purchased were rated investment grade at the time of purchase. Aflac Japan's investments in yen-denominated privately issued securities consist primarily of non-Japanese issuers and have longer maturities, thereby allowing us to improve our asset/liability matching and our overall investment returns. These securities were generally either privately negotiated arrangements or were issued under medium-term note programs and have standard documentation commensurate with credit ratings of the issuer, except when internal credit analysis indicates that additional protective and/or event-risk covenants were required. Many of these investments have protective covenants appropriate to the specific investment. These may include a prohibition of certain activities by the borrower, maintenance of certain financial measures, and specific conditions impacting the payment of our notes.





### Below-Investment-Grade and Split-Rated Securities

We use specific criteria to judge the credit quality of both existing and prospective investments. The ratings referenced in the tables below are based on the ratings designations provided by the major credit rating agencies (Moody's, S&P, and Fitch) or, if not rated, are determined based on our internal credit analysis of such securities. When the ratings issued by the rating agencies differ, we utilize the second lowest rating, regardless of how many of the three rating agencies actually rated the instrument. Split-rated securities are those where the ratings are not equivalent and one or more of the ratings is investment grade and one or more is below investment grade. For these split-rated securities, if there are only two ratings assigned by the credit rating agencies, we take the lower below-investment-grade rating. If there are three ratings assigned, and two of the three are below investment grade, we consider it a below-investment grade security. If there are three ratings and two are investment grade, we consider it an investment grade security unless our evaluation and assessment shows a below-investment-grade rating is warranted despite two of the three rating agencies rating it investment grade.

Our portfolio of below-investment-grade securities includes debt securities purchased while the issuer was rated investment grade plus other loans and bonds purchased as part of an allocation to that segment of the market. The following is our below-investment-grade exposure in accordance with the above described rating methodology.

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Below-Investment-Grade Securities

| (In millions)  | June 30, 2016 |                |            |                        | December 31, 2015 |                |            |                       |
|--|---------------|----------------|------------|------------------------|-------------------|----------------|------------|-----------------------|
|  | Par Value     | Amortized Cost | Fair Value | Unrealized Gain (Loss) | Par Value         | Amortized Cost | Fair Value | Unrealized Gain(Loss) |
| Investcorp Capital Limited                                     | \$410         | \$ 409         | \$382      | \$ (27 )               | \$357             | \$ 357         | \$324      | \$ (33 )              |
| Republic of Tunisia  | 360           | 217            | 278        | 61                     | 307               | 185            | 243        | 58                    |
| Navient Corp   | 321           | 169            | 183        | 14                     | 279               | 148            | 155        | 7                     |
| UPM-Kymmene  | 301           | 297            | 274        | (23 )                  | 257               | 257            | 252        | (5 )                  |
| KLM Royal Dutch Airlines <sup>(1)</sup>                        | 291           | 214            | 234        | 20                     | 249               | 183            | 205        | 22                    |
| Barclays Bank PLC <sup>(1)</sup>                               | 259           | 167            | 217        | 50                     | 230               | 148            | 228        | 80                    |
| Deutsche Postbank AG   | 233           | 233            | 177        | (56 )                  | 199               | 199            | 175        | (24 )                 |
| Telecom Italia SpA   | 194           | 194            | 236        | 42                     | 166               | 166            | 214        | 48                    |
| Generalitat de Catalunya                                       | 175           | 64             | 139        | 75                     | 149               | 55             | 126        | 71                    |
| Diamond Offshore Drilling Inc.                                 | 129           | 151            | 98         | (53 )                  | *                 | *              | *          | *                     |
| IKB Deutsche Industriebank AG                                  | 126           | 53             | 96         | 43                     | 108               | 46             | 79         | 33                    |
| Noble Holdings International Ltd.                              | 104           | 111            | 66         | (45 )                  | *                 | *              | *          | *                     |
| Alcoa, Inc.  | 100           | 91             | 93         | 2                      | 100               | 77             | 81         | 4                     |
| Societe Generale <sup>(1)</sup>                                | 97            | 71             | 90         | 19                     | 83                | 61             | 73         | 12                    |
| Petrobras International Finance Company                        | 91            | 96             | 79         | (17 )                  | 91                | 88             | 64         | (24 )                 |
| Cenovus Energy Inc.  | 75            | 81             | 66         | (15 )                  | *                 | *              | *          | *                     |
| Teck Resources Ltd.  | 70            | 74             | 53         | (21 )                  | 70                | 69             | 32         | (37 )                 |
| Transocean Inc.  | 68            | 74             | 45         | (29 )                  | 68                | 71             | 38         | (33 )                 |
| Weatherford Bermuda  | 59            | 60             | 44         | (16 )                  | 94                | 92             | 70         | (22 )                 |
| Eskom Holdings Limited   | 50            | 50             | 49         | (1 )                   | 50                | 50             | 43         | (7 )                  |
| Votorantim Overseas Trading IV Ltd.                            | 50            | 50             | 53         | 3                      | *                 | *              | *          | *                     |
| Commerzbank AG (includes Dresdner Bank)                        | *             | *              | *          | *                      | 332               | 213            | 321        | 108                   |
| DEPFA Bank PLC   | 0             | 0              | 0          | 0                      | 166               | 166            | 166        | 0                     |
| Other Issuers (below \$50 million in par value) <sup>(2)</sup> | 306           | 306            | 271        | (35 )                  | 333               | 306            | 277        | (29 )                 |
| Subtotal <sup>(3)</sup>  | 3,869         | 3,232          | 3,223      | (9 )                   | 3,688             | 2,937          | 3,166      | 229                   |
| Senior secured bank loans <sup>(4)</sup>                       | 1,834         | 1,994          | 1,817      | (177 )                 | 1,400             | 1,327          | 1,362      | 35                    |
| High yield corporate bonds <sup>(5)</sup>                      | 652           | 668            | 645        | (23 )                  | 609               | 621            | 581        | (40 )                 |
| Grand Total  | \$6,355       | \$ 5,894       | \$5,685    | \$ (209 )              | \$5,697           | \$ 4,885       | \$5,109    | \$ 224                |

\* Investment grade at respective reporting date

(1) Includes perpetual security

(2) Includes 15 issuers in 2016 and 2015

(3) Securities initially purchased as investment grade, but have subsequently been downgraded to below investment grade

(4) Includes 195 issuers in 2016 and 201 in 2015; all issuers below \$25 million in par value

<sup>(5)</sup> Includes 65 issuers in 2016 and 57 in 2015; all issuers below \$25 million in par value

We invest in senior secured bank loans primarily to U.S. corporate borrowers, most of which have below-investment-grade ratings. The program is managed externally by third party firms specializing in this asset class. This mandate requires a minimum average credit quality of BB-/Ba3. The objectives of this program include enhancing the yield on invested assets, achieving further diversification of credit risk, and mitigating the risk of rising interest rates through the acquisition of floating rate assets. Our investments in this program totaled \$2.1 billion at June 30, 2016, compared with \$1.4 billion at December 31, 2015, on an amortized cost basis.

In 2015, we increased our allocation to higher yielding corporate bonds within the Aflac Japan and Aflac U.S. portfolios. Most of these securities were rated below-investment-grade at the time of purchase, but we also purchased several that were rated investment grade which, because of market pricing, offer yields commensurate with below-investment-grade risk profiles. The objective of this allocation was to enhance our yield on invested assets and further diversify our credit risk. All investments must have a minimum rating of low BB using our above described rating methodology and are managed by our internal credit portfolio management team.

Excluding the senior secured bank loans and certain high yield corporate bonds discussed above that were rated below investment grade when initially purchased, below-investment-grade debt and perpetual securities represented 2.9% of total debt and perpetual securities at June 30, 2016, compared with 3.1% at December 31, 2015, on an amortized cost basis. Debt and perpetual securities classified as below investment grade at June 30, 2016 and December 31, 2015 were generally reported as available for sale and carried at fair value.

The following table shows the 10 largest holdings with a split rating, and includes the determination between investment grade and below investment grade based on the above methodology as of June 30, 2016.

#### Split-Rated Securities

| (In millions)                           | Amortized Investment-Grade |                        |
|---|----------------------------|------------------------|
|   | Cost                       | Status                 |
| Commerzbank AG (includes Dresdner Bank) | \$ 250                     | Investment Grade       |
| Telecom Italia SpA                      | 194                        | Below Investment Grade |
| Alberta Energy Company LTD.             | 172                        | Investment Grade       |
| Vale SA                                 | 169                        | Investment Grade       |
| Diamond Offshore Drilling Inc.          | 151                        | Below Investment Grade |
| Devon Energy Corp.                      | 141                        | Investment Grade       |
| Marathon Oil Corp.                      | 138                        | Investment Grade       |
| Energias de Portugal SA (EDP)           | 131                        | Investment Grade       |
| Barclays Bank PLC <sup>(1)</sup>        | 120                        | Below Investment Grade |
| Time Warner Cable Inc.                  | 118                        | Investment Grade       |

<sup>(1)</sup> Includes perpetual security

Split-rated securities, excluding the senior secured bank loan investments and high yield corporate bonds discussed above, totaled \$2.4 billion and represented 2.2% of total debt and perpetual securities, at amortized cost, at June 30, 2016, compared with \$1.3 billion and 1.3%, respectively, at December 31, 2015. The increase in split-rated securities is primarily related to negative ratings actions against many issuers operating in the energy sector (see the preceding Oil and Gas subsection of this MD&A for further discussion).

#### Derivative Counterparties

For the foreign currency and credit default swaps associated with our VIE investments for which we are the primary beneficiary, we bear the risk of foreign exchange and/or credit loss due to counterparty default even though we are not a direct counterparty to those contracts. We are a direct counterparty to the foreign currency swaps that we have on certain of our senior notes and subordinated debentures; foreign currency forwards; foreign currency options; and interest rate swaptions, therefore we are exposed to credit risk in the event of nonperformance by the counterparties in those contracts. The risk of counterparty default for our VIE and senior note and subordinated debenture swaps, foreign currency forwards and options, and swaptions is mitigated by collateral posting requirements the counterparty must meet. If collateral posting agreements are not in place, the counterparty risk associated with foreign currency forwards and foreign currency options is the risk that at expiry of the contract, the counterparty is unable to deliver the agreed upon amount of yen at the agreed upon price or delivery date, thus exposing the company to additional unhedged exposure to U.S. dollars in the Aflac Japan investment portfolio. See Note 4 of the Notes to the Consolidated Financial Statements for more information.



## Equity Risk

Market prices for equity securities are subject to fluctuation and consequently the amount realized in the subsequent sale of an investment may significantly differ from the reported market value. Fluctuation in the market price of a security may result from the relative price of alternative investments and general market conditions. These fluctuations could impact the Company's consolidated results of operations or financial condition.

## Other-than-temporary Impairment

See Note 3 of the Notes to the Consolidated Financial Statements for a discussion of our impairment policy.

## Unrealized Investment Gains and Losses

The following table provides details on amortized cost, fair value and unrealized gains and losses for our investments in fixed maturities, perpetual securities, and equity securities by investment-grade status as of June 30, 2016.

| (In millions)   | Total Amortized Cost | Total Fair Value | Percentage of Total Fair Value | Gross Unrealized Gains | Gross Unrealized Losses |
|---|----------------------|------------------|--------------------------------|------------------------|-------------------------|
| Available-for-sale fixed maturities and perpetual securities: |                      |                  |                                |                        |                         |
| Investment-grade securities                                   | \$66,021             | \$76,433         | 57.9 %                         | \$ 11,114              | \$ 702                  |
| Below-investment-grade securities                             | 5,894                | 5,685            | 4.3                            | 358                    | 567                     |
| Held-to-maturity fixed maturities:                            |                      |                  |                                |                        |                         |
| Investment-grade securities                                   | 38,346               | 48,796           | 36.9                           | 10,507                 | 57                      |
| Equity securities   | 1,245                | 1,197            | 0.9                            | 46                     | 94                      |
| Total   | \$111,506            | \$132,111        | 100.0 %                        | \$ 22,025              | \$ 1,420                |

The following table presents an aging of fixed maturities, perpetual securities, and equity securities in an unrealized loss position as of June 30, 2016.

## Aging of Unrealized Losses

| (In millions)   | Total Amortized Cost | Total Unrealized Loss | Less than Six Months |                 | Six Months to Less than 12 Months |                 | 12 Months or Longer |                 |
|---|----------------------|-----------------------|----------------------|-----------------|-----------------------------------|-----------------|---------------------|-----------------|
|   |                      |                       | Amortized Cost       | Unrealized Loss | Amortized Cost                    | Unrealized Loss | Amortized Cost      | Unrealized Loss |
| Available-for-sale fixed maturities and perpetual securities: |                      |                       |                      |                 |                                   |                 |                     |                 |
| Investment-grade securities                                   | \$ 9,759             | \$ 702                | \$ 1,894             | \$ 97           | \$ 726                            | \$ 49           | \$ 7,139            | \$ 556          |
| Below-investment-grade securities                             | 4,134                | 567                   | 2,241                | 196             | 60                                | 4               | 1,833               | 367             |
| Held-to-maturity fixed maturities:                            |                      |                       |                      |                 |                                   |                 |                     |                 |
| Investment-grade securities                                   | 1,846                | 57                    | 146                  | 1               | 97                                | 2               | 1,603               | 54              |
| Equity securities   | 772                  | 94                    | 605                  | 63              | 167                               | 31              | 0                   | 0               |
| Total   | \$ 16,511            | \$ 1,420              | \$ 4,886             | \$ 357          | \$ 1,050                          | \$ 86           | \$ 10,575           | \$ 977          |

The following table presents a distribution of unrealized losses on fixed maturities, perpetual securities, and equity securities by magnitude as of June 30, 2016.



## Percentage Decline From Amortized Cost

| (In millions)   | Total<br>Amortized<br>Cost | Total<br>Unrealized<br>Loss | Less than 20%     |                    | 20% to 50%        |                    | Greater than<br>50% |                    |
|---|----------------------------|-----------------------------|-------------------|--------------------|-------------------|--------------------|---------------------|--------------------|
|   |                            |                             | Amortized<br>Cost | Unrealized<br>Loss | Amortized<br>Cost | Unrealized<br>Loss | Amortized<br>Cost   | Unrealized<br>Loss |
| Available-for-sale fixed<br>maturities and<br>perpetual securities: |                            |                             |                   |                    |                   |                    |                     |                    |
| Investment-grade<br>securities                                      | \$ 9,759                   | \$ 702                      | \$8,963           | \$ 500             | \$796             | \$ 202             | \$ 0                | \$ 0               |
| Below-<br>investment-grade<br>securities                            | 4,134                      | 567                         | 3,251             | 293                | 883               | 274                | 0                   | 0                  |
| Held-to-maturity<br>fixed maturities:                               |                            |                             |                   |                    |                   |                    |                     |                    |
| Investment-grade<br>securities                                      | 1,846                      | 57                          | 1,846             | 57                 | 0                 | 0                  | 0                   | 0                  |
| Equity securities   | 772                        | 94                          | 605               | 53                 | 167               | 41                 | 0                   | 0                  |
| Total   | \$ 16,511                  | \$ 1,420                    | \$14,665          | \$ 903             | \$1,846           | \$ 517             | \$ 0                | \$ 0               |

The following table presents the 10 largest unrealized loss positions in our portfolio as of June 30, 2016.

| (In millions)                                   | Credit<br>Rating | Amortized<br>Cost | Fair<br>Value | Unrealized<br>Loss |
|---|------------------|-------------------|---------------|--------------------|
| AXA <sup>(1)</sup>                              | BBB              | \$ 313            | \$253         | \$ (60 )           |
| Deutsche Postbank AG                            | BB               | 233               | 177           | (56 )              |
| Diamond Offshore Drilling Inc.                  | BB               | 151               | 98            | (53 )              |
| Noble Holdings International Ltd.               | B                | 111               | 66            | (45 )              |
| Kommunal Lanspensjonskasse (KLP) <sup>(1)</sup> | BBB              | 238               | 198           | (40 )              |
| Transocean Inc.                                 | B                | 74                | 45            | (29 )              |
| Investcorp Capital Limited                      | BB               | 409               | 382           | (27 )              |
| Koninklijke Ahold NV                            | BBB              | 335               | 311           | (24 )              |
| UPM-Kymmene                                     | BB               | 297               | 274           | (23 )              |
| National Oilwell Varco Inc.                     | BBB              | 116               | 95            | (21 )              |

<sup>(1)</sup> Includes perpetual security

Generally, declines in fair values can be a result of changes in interest rates, yen/dollar exchange rate, and changes in net spreads driven by a broad market move or a change in the issuer's underlying credit quality. At times during the first six months of 2016, we saw market volatility at elevated levels, especially in the energy and commodity-related sectors. As we believe these issuers have the ability to continue making timely payments of principal and interest, we view these changes in fair value to be temporary and do not believe it is necessary to impair the carrying value of these securities. See the Unrealized Investment Gains and Losses section in Note 3 of the Notes to the Consolidated Financial Statements for further discussions of unrealized losses related to financial institutions, including perpetual securities, and other corporate investments.

## Investment Valuation and Cash

We estimate the fair values of our securities on a monthly basis. We monitor the estimated fair values obtained from our custodian, pricing vendors and brokers for consistency from month to month, while considering current market conditions. We also periodically discuss with our custodian and pricing brokers and vendors the pricing techniques



they use to monitor the consistency of their approach and periodically assess the appropriateness of the valuation level assigned to the values obtained from them. If a fair value appears unreasonable, we will re-examine the inputs and assess the reasonableness of the pricing data with the vendor. Additionally, we may compare the inputs to relevant market indices and other performance measurements. The output of this analysis is presented to the Company's Valuation and Classification Subcommittee (VCS). Based on the analysis provided to the VCS, the valuation is confirmed or may be revised if there is evidence of a more appropriate estimate of fair value based on available market data. We have

performed verification of the inputs and calculations in any valuation models to confirm that the valuations represent reasonable estimates of fair value.

For those investments accounted for as loan receivables, we record those investments at amortized cost on the acquisition date and carry at adjusted amortized cost. The adjusted amortized cost of the loan receivables reflects allowances for expected incurred losses estimated based on past events and current economic conditions as of each reporting date. See the Loans and Loan Receivables section in Note 3 of the Notes to the Consolidated Financial Statements for further discussion of these investments.

Cash and cash equivalents totaled \$3.7 billion, or 2.9% of total investments and cash, as of June 30, 2016, compared with \$4.4 billion, or 4.1%, at December 31, 2015. For a discussion of the factors affecting our cash balance, see the Operating Activities, Investing Activities and Financing Activities subsections of this MD&A.

For additional information concerning our investments, see Notes 3, 4, and 5 of the Notes to the Consolidated Financial Statements.

#### Deferred Policy Acquisition Costs

The following table presents deferred policy acquisition costs by segment.

| (In millions) | June 30, | December 31, | % Change              |
|---------------|----------|--------------|-----------------------|
|               | 2016     | 2015         |                       |
| Aflac Japan   | \$6,391  | \$ 5,370     | 19.0 % <sup>(1)</sup> |
| Aflac U.S.    | 3,161    | 3,141        | .6                    |
| Total         | \$9,552  | \$ 8,511     | 12.2 %                |

<sup>(1)</sup>Aflac Japan's deferred policy acquisition costs increased 1.5% in yen during the six months ended June 30, 2016.

See Note 6 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015 for additional information on our deferred policy acquisition costs.

#### Policy Liabilities

The following table presents policy liabilities by segment.

| (In millions)                            | June 30,  | December 31, | % Change              |
|--|-----------|--------------|-----------------------|
|  | 2016      | 2015         |                       |
| Aflac Japan                              | \$93,763  | \$ 78,460    | 19.5 % <sup>(1)</sup> |
| Aflac U.S.                               | 10,036    | 9,815        | 2.3                   |
| Other                                    | 78        | 43           | 81.4                  |
| Intercompany eliminations <sup>(2)</sup> | (811 )    | (687 )       | 18.0                  |
| Total                                    | \$103,066 | \$ 87,631    | 17.6 %                |

<sup>(1)</sup> Aflac Japan's policy liabilities increased 2.0% in yen during the six months ended June 30, 2016.

<sup>(2)</sup> Elimination entry necessary due to recapture of a portion of policy liabilities ceded externally, as a result of the reinsurance retrocession transaction as described in Note 6 of the Notes to the Consolidated Financial Statements.

#### Notes Payable

As of January 1, 2016, we adopted updated accounting guidance related to the presentation of debt issuance costs and have reclassified debt issuance costs related to a debt liability as a direct deduction from the carrying amount of that debt liability. Prior year amounts have been adjusted to reflect the current year adoption. See Note 1 of the accompanying Notes to the Consolidated Financial Statements for additional information.

Notes payable totaled \$5.0 billion at June 30, 2016 and December 31, 2015.

See Note 7 of the accompanying Notes to the Consolidated Financial Statements for additional information on our notes payable.



## Benefit Plans

Aflac Japan and Aflac U.S. have various benefit plans. For additional information on our Japanese and U.S. plans, see Note 10 of the accompanying Notes to the Consolidated Financial Statements and Note 14 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015.

## Policyholder Protection Corporation

The Japanese insurance industry has a policyholder protection system that provides funds for the policyholders of insolvent insurers. Legislation enacted regarding the framework of the Life Insurance Policyholder Protection Corporation (LIPPC) included government fiscal measures supporting the LIPPC. On December 27, 2011, Japan's FSA announced the plans to enhance the stability of the LIPPC by extending the government's fiscal support of the LIPPC through March 2017. Accordingly, the FSA submitted legislation to the Diet on January 27, 2012 to extend the government's fiscal support framework, and the legislation was approved on March 30, 2012. Effective April 2014, the annual LIPPC contribution amount for the total life industry was lowered from 40 billion yen to 33 billion yen.

## Hedging Activities

### Net Investment Hedge

Our primary exposure to be hedged is our investment in Aflac Japan, which is affected by changes in the yen/dollar exchange rate. To mitigate this exposure, we have taken the following courses of action. First, Aflac Japan maintains certain unhedged U.S. dollar-denominated securities, which serve as an economic currency hedge of a portion of our investment in Aflac Japan. Second, we have designated the majority of the Parent Company's yen-denominated liabilities (Samurai and Uridashi notes) as non-derivative hedging instruments and certain foreign currency forwards and options as derivative hedges of our net investment in Aflac Japan. We make our net investment hedge designation at the beginning of each quarter. If the total of the designated Parent Company non-derivative and derivatives notional is equal to or less than our net investment in Aflac Japan, the hedge is deemed to be effective, and the exchange effect on the yen-denominated liabilities and the change in estimated fair value of the derivatives are reported in the unrealized foreign currency component of other comprehensive income. We estimate that if the designated net investment hedge positions exceeded our net investment in Aflac Japan by 10 billion yen, we would report a foreign exchange gain/loss of approximately \$1 million for every 1% yen weakening/strengthening in the end-of-period yen/dollar exchange rate. Our net investment hedge was effective during the three- and six-month periods ended June 30, 2016 and 2015, respectively.

The yen net asset figure calculated for hedging purposes differs from the yen-denominated net asset position as discussed in the Currency Risk subsection of MD&A. As disclosed in that subsection, the consolidation of the underlying assets in certain VIEs requires that we derecognize our yen-denominated investment in the VIE and recognize the underlying fixed-maturity or perpetual securities and cross-currency swaps. While these U.S. dollar investments will create foreign currency fluctuations, the combination of the U.S. dollar-denominated investment and the cross-currency swap economically creates a yen-denominated investment that qualifies for inclusion as a component of our investment in Aflac Japan. Similarly, the combination of the U.S. corporate bonds and the foreign currency forwards and options that we have entered into, as discussed in the Aflac Japan Investment subsection of MD&A, economically creates a yen-denominated investment that qualifies for inclusion as a component of our investment in Aflac Japan.

The dollar values of our yen-denominated net assets, including economic yen-denominated investments for net investment hedging purposes as discussed above, are summarized as follows (translated at end-of-period exchange rates):

| (In millions)   | June 30,<br>2016 | December 31,<br>2015 |
|---|------------------|----------------------|
| Aflac Japan net assets                                | \$ 19,160        | \$ 13,558            |
| Aflac Japan unhedged dollar-denominated net assets    | (9,400 )         | (8,111 )             |
| Consolidated yen-denominated net assets (liabilities) | \$ 9,760         | \$ 5,447             |

For the hedge of our net investment in Aflac Japan, we have designated certain of the Parent Company's yen-denominated liabilities, certain unhedged U.S. dollar investments and foreign currency forwards and options as a hedge of our net investment in Aflac Japan. Our consolidated yen-denominated net asset position was partially hedged

at \$1.8 billion as of June 30, 2016, compared with \$1.2 billion as of December 31, 2015.

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## Cash Flow Hedges

We had freestanding derivative instruments related to our consolidated VIE investments that are reported in the consolidated balance sheet at fair value within other assets and other liabilities. As of June 30, 2016, two of the freestanding swaps that are used within VIEs to hedge the risk arising from changes in foreign currency exchange rates qualified for hedge accounting.

## Fair Value Hedges

We have entered into foreign currency forwards and options to mitigate the foreign exchange risk associated with new investments in U.S. dollar-denominated fixed-maturities that support yen-denominated liabilities within our Aflac Japan segment.

At times we have entered into interest rate swaptions to mitigate the interest rate risk associated with our U.S. dollar-denominated fixed-maturities that support yen-denominated liabilities within our Aflac Japan segment.

See Note 4 of the Notes to the Consolidated Financial Statements for additional information on our hedging activities.

## Off-Balance Sheet Arrangements

As of June 30, 2016, we had no material letters of credit, standby letters of credit, guarantees or standby repurchase obligations. See Note 15 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015, for information on material unconditional purchase obligations that are not recorded on our balance sheet.

## CAPITAL RESOURCES AND LIQUIDITY

Aflac provides the primary sources of liquidity to the Parent Company through dividends and management fees. The following table presents the amounts provided for the six-month periods ending June 30.

| Liquidity Provided by Aflac to Parent Company<br>(In millions) | 2016  | 2015  |
|--|-------|-------|
| Dividends declared or paid by Aflac                            | \$626 | \$746 |
| Management fees paid by Aflac                                  | 124   | 158   |

The primary uses of cash by the Parent Company are shareholder dividends, the repurchase of its common stock and interest on its outstanding indebtedness and operating expenses. The Parent Company's sources and uses of cash are reasonably predictable and are not expected to change materially in the future. For additional information, see the Financing Activities subsection of this MD&A.

The Parent Company also accesses debt security markets to provide additional sources of capital. We filed a shelf registration statement with the SEC in May 2015 that allows us to issue an indefinite amount of senior and subordinated debt, in one or more series, from time to time until May 2018. We believe outside sources for additional debt and equity capital, if needed, will continue to be available. For additional information, see Note 7 of the Notes to the Consolidated Financial Statements.

The principal sources of cash for our insurance operations are premiums and investment income. The primary uses of cash by our insurance operations are investments, policy claims, commissions, operating expenses, income taxes and payments to the Parent Company for management fees and dividends. Both the sources and uses of cash are reasonably predictable.

When making an investment decision, our first consideration is based on product needs. Our investment objectives provide for liquidity through the purchase of investment-grade debt securities. These objectives also take into account

duration matching, and because of the long-term nature of our business, we have adequate time to react to changing cash flow needs.

As a result of policyholder aging, claims payments are expected to gradually increase over the life of a policy. Therefore, future policy benefit reserves are accumulated in the early years of a policy and are designed to help fund

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future claims payments. We expect our future cash flows from premiums and our investment portfolio to be sufficient to meet our cash needs for benefits and expenses.

In March 2016, the Parent Company entered into a three-year senior unsecured revolving credit facility agreement with a group of financial institutions that provides for borrowings of up to 100.0 billion yen on a revolving basis. Borrowings bear interest at a rate per annum equal to the Tokyo interbank market rate (TIBOR) plus, at our option, either (a) the applicable TIBOR margin during the period from the closing date to the commitment termination date or (b) the applicable TIBOR margin during the term out period. The applicable margin ranges between .35% and .75% during the period from the closing date to the commitment termination date and .70% and 1.50% during the term out period, depending on the Parent Company's debt ratings as of the date of determination. In addition, the Parent Company is required to pay a facility fee on the commitments ranging between .30% and .50%, also based on the Parent Company's debt ratings as of the date of determination. Borrowings under this credit agreement may be used for general corporate purposes, including a capital contingency plan for the operations of the Parent Company, and will expire on the earlier of (a) March 31, 2019, or (b) the date the commitments are terminated pursuant to an event of default, as such term is defined in the credit agreement. The credit facility requires compliance with certain financial covenants on a quarterly basis. As of June 30, 2016, we did not have any borrowings outstanding under our 100.0 billion yen revolving credit agreement.

The Parent Company and Aflac have a 364-day uncommitted bilateral line of credit with a third party that provides for borrowings in the amount of \$100 million. Borrowings will bear interest at the rate quoted by the bank and agreed upon at the time of making such loan and will have a three-month maturity period. There are no related facility fees, upfront expenses or financial covenant requirements. Borrowings under this credit agreement may be used for general corporate purposes. Borrowings under the financing agreement will mature no later than three months after the last drawdown date of October 15, 2016. As of June 30, 2016, we did not have any borrowings outstanding under our \$100 million credit agreement.

The Parent Company and Aflac have a five-year senior unsecured revolving credit facility agreement with a syndicate of financial institutions that provides for borrowings of up to 55.0 billion yen or the equivalent of yen in U.S. dollars on a revolving basis. This credit agreement provides for borrowings in Japanese yen or the equivalent of Japanese yen in U.S. dollars on a revolving basis. Borrowings bear interest at a rate per annum equal to, at our option, either (a) a eurocurrency rate determined by reference to the London Interbank Offered Rate (LIBOR) for the interest period relevant to such borrowing adjusted for certain additional costs or (b) a base rate determined by reference to the highest of (1) the federal funds effective rate plus  $\frac{1}{2}$  of 1%, (2) the rate of interest for such day announced by Mizuho Bank, Ltd. as its prime rate and (3) the eurocurrency rate for an interest period of one month plus 1.00%, in each case plus an applicable margin. The applicable margin ranges between .79% and 1.275% for eurocurrency rate borrowings and 0.0% and .275% for base rate borrowings, depending on the Parent Company's debt ratings as of the date of determination. In addition, the Parent Company and Aflac are required to pay a facility fee on the commitments ranging between .085% and .225%, also based on the Parent Company's debt ratings as of the date of determination. Borrowings under the amended and restated credit facility may be used for general corporate purposes, including a capital contingency plan for the operations of the Parent Company and Aflac. The amended and restated credit facility requires compliance with certain financial covenants on a quarterly basis and will expire on the earlier of (a) September 18, 2020, or (b) the date the commitments are terminated pursuant to an event of default, as such term is defined in the credit agreement. As of June 30, 2016, we did not have any borrowings outstanding under our 55.0 billion yen revolving credit agreement.

The Parent Company and Aflac have an uncommitted bilateral line of credit with a third party that provides for borrowings in the amount of \$50 million. Borrowings will bear interest at the rate quoted by the bank and agreed upon at the time of making such loan and will have a three-month maturity period. There are no related facility fees, upfront expenses or financial covenant requirements. Borrowings under this credit agreement may be used for general corporate purposes. As of June 30, 2016, we did not have any borrowings outstanding under our \$50 million credit



agreement.

Our financial statements convey our financing arrangements during the periods presented. We have not engaged in material intra-period short-term financings during the periods presented that are not otherwise reported in our balance sheet. We were in compliance with all of the covenants of our notes payable and lines of credit at June 30, 2016. We have not entered into transactions involving the transfer of financial assets with an obligation to repurchase financial assets that have been accounted for as a sale under applicable accounting standards, including securities lending transactions. See Notes 3 and 4 of the Notes to the Consolidated Financial Statements and Note 1 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015, for more information on our securities lending and derivative activities. With the exception of disclosed activities in those referenced footnotes, we do not have a known trend, demand, commitment, event or uncertainty that would reasonably result in our liquidity increasing or decreasing by a material amount. Our cash and cash equivalents include unrestricted cash on hand, money

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market instruments, and other debt instruments with a maturity of 90 days or less when purchased, all of which has minimal market, settlement or other risk exposure.

#### Consolidated Cash Flows

We translate cash flows for Aflac Japan's yen-denominated items into U.S. dollars using weighted-average exchange rates. In periods when the yen weakens, translating yen into dollars causes fewer dollars to be reported. When the yen strengthens, translating yen into dollars causes more dollars to be reported.

The following table summarizes consolidated cash flows by activity for the six-month periods ended June 30.

| (In millions)                                | 2016     | 2015      |
|--|----------|-----------|
| Operating activities                         | \$2,854  | \$3,103   |
| Investing activities                         | (2,429 ) | (3,566 )  |
| Financing activities                         | (1,281 ) | (1,087 )  |
| Exchange effect on cash and cash equivalents | 206      | (5 )      |
| Net change in cash and cash equivalents      | \$(650 ) | \$(1,555) |

#### Operating Activities

The following table summarizes operating cash flows by source for the six-month periods ended June 30.

| (In millions)                   | 2016    | 2015    |
|---------------------------------|---------|---------|
| Aflac Japan                     | \$2,207 | \$2,417 |
| Aflac U.S. and other operations | 647     | 686     |
| Total                           | \$2,854 | \$3,103 |

#### Investing Activities

Operating cash flow is primarily used to purchase debt securities to meet future policy obligations. The following table summarizes investing cash flows by source for the six-month periods ended June 30.

| (In millions)                   | 2016      | 2015      |
|---------------------------------|-----------|-----------|
| Aflac Japan                     | \$(1,482) | \$(3,336) |
| Aflac U.S. and other operations | (947 )    | (230 )    |
| Total                           | \$(2,429) | \$(3,566) |

Prudent portfolio management dictates that we attempt to match the duration of our assets with the duration of our liabilities. Currently, when our fixed-maturity securities and perpetual securities mature, the proceeds may be reinvested at a yield below that required for the accretion of policy benefit liabilities on policies issued in earlier years. However, the long-term nature of our business and our strong cash flows provide us with the ability to minimize the effect of mismatched durations and/or yields identified by various asset adequacy analyses. When needed or when market opportunities arise, we dispose of selected fixed-maturity and perpetual securities that are available for sale to improve the duration matching of our assets and liabilities, improve future investment yields, and/or re-balance our portfolio. As a result, dispositions before maturity can vary significantly from year to year. Dispositions before maturity were approximately 1% and 2% of the year-to-date average investment portfolio of fixed maturities and perpetual securities available for sale during the six-month periods ended June 30, 2016 and 2015, respectively.

#### Financing Activities

Consolidated cash used by financing activities was \$1.3 billion in the first six months of 2016, compared with consolidated cash used by financing activities of \$1.1 billion for the same period of 2015.

Cash returned to shareholders through dividends and treasury stock purchases was \$1.3 billion during the six-month period ended June 30, 2016, compared with \$1.2 billion during the six-month period ended June 30, 2015.

We were in compliance with all of the covenants of our notes payable and lines of credit at June 30, 2016.

The following tables present a summary of treasury stock activity during the six-month periods ended June 30.

#### Treasury Stock Purchased

| (In millions of dollars and thousands of shares) | 2016    | 2015   |
|--|---------|--------|
| Treasury stock purchases                         | \$1,014 | \$ 848 |
| Number of shares purchased:                      |         |        |
| Open market                                      | 16,026  | 13,534 |
| Other  | 224     | 214    |
| Total shares purchased                           | 16,250  | 13,748 |

#### Treasury Stock Issued

| (In millions of dollars and thousands of shares) | 2016  | 2015  |
|--|-------|-------|
| Stock issued from treasury:                      |       |       |
| Cash financing                                   | \$ 19 | \$ 20 |
| Noncash financing                                | 34    | 34    |
| Total stock issued from treasury                 | \$ 53 | \$ 54 |
| Number of shares issued                          | 944   | 986   |

During the first six months of 2016, we repurchased 16.0 million shares of our common stock for \$1.0 billion as part of our share repurchase program. As of June 30, 2016, a remaining balance of 32.3 million shares of our common stock was available for purchase under share repurchase authorizations by our board of directors. We currently plan to repurchase \$1.4 billion of our common stock in 2016, with the majority already purchased in the first half of the year.

Cash dividends paid to shareholders were \$.41 per share in the second quarter of 2016, compared with \$.39 per share in the second quarter of 2015. The following table presents the dividend activity for the six-month periods ended June 30.

| (In millions)                                 | 2016  | 2015  |
|---|-------|-------|
| Dividends paid in cash                        | \$330 | \$328 |
| Dividends through issuance of treasury shares | 12    | 12    |
| Total dividends to shareholders               | \$342 | \$340 |

In July 2016, the board of directors declared the third quarter cash dividend of \$.41 per share, an increase of 5.1% compared with the same period in 2015. The dividend is payable on September 1, 2016, to shareholders of record at the close of business on August 24, 2016.

#### Regulatory Restrictions

Aflac is domiciled in Nebraska and is subject to its laws and regulations. A life insurance company's statutory capital and surplus is determined according to rules prescribed by the National Association of Insurance Commissioners (NAIC), as modified by the insurance department in the insurance company's state of domicile. Statutory accounting rules are different from U.S. GAAP and are intended to emphasize policyholder protection and company solvency. Similar laws apply in New York and South Carolina, the domiciliary jurisdictions of the Parent Company's other insurance subsidiaries, Aflac New York and CAIC. The continued long-term growth of our business may require increases in the statutory capital and surplus of our insurance operations. Aflac's insurance operations may secure additional statutory capital through various sources, such as internally generated statutory earnings, equity contributions by the Parent Company from funds generated through debt or equity offerings, or reinsurance transactions. The NAIC's risk-based capital (RBC) formula is used by insurance regulators to help identify inadequately capitalized insurance companies. The RBC formula quantifies insurance risk, business risk, asset risk and interest rate risk by weighing the types and mixtures of risks inherent in the insurer's operations. As of June 30,

2016, Aflac's RBC ratio remains high and reflects a strong capital and surplus position. The maximum amount of dividends that can be paid to the Parent Company by Aflac without prior approval of Nebraska's director of insurance is the greater of the net income from operations, which excludes net realized investment gains, for the previous year determined under statutory accounting principles, or 10% of statutory capital and surplus as of

the previous year-end. Dividends declared by Aflac during 2016 in excess of \$2.3 billion would require such approval.

In addition to limitations and restrictions imposed by U.S. insurance regulators, Japan's FSA may not allow profit repatriations from Aflac Japan if the transfers would cause Aflac Japan to lack sufficient financial strength for the protection of policyholders. The FSA maintains its own solvency standard which is quantified through the solvency margin ratio (SMR). Aflac Japan's SMR is sensitive to interest rate and foreign exchange rate changes, therefore we continue to evaluate alternatives for reducing this sensitivity. In the event of a rapid change in interest rates, we have two senior unsecured revolving credit facilities in the amounts of 100 billion yen and 55 billion yen, respectively, and a committed reinsurance facility in the amount of approximately 110 billion yen as a capital contingency plan. (See Notes 8 and 9 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015 for additional information on our capital contingency plan.) We have already undertaken various measures to mitigate the sensitivity of Aflac Japan's SMR. For example, we employ policy reserve matching (PRM) investment strategies, which is a Japan-specific accounting treatment that reduces SMR interest rate sensitivity since PRM-designated investments are carried at amortized cost consistent with corresponding liabilities. For U.S. GAAP, PRM investments are categorized as available-for-sale. In the first quarter of 2015, Aflac Japan entered into a quota share arrangement to cede a portion of hospital benefits of one of our closed products. Under this coinsurance indemnity type of reinsurance, Aflac Japan released approximately 130 billion yen of FSA reserves. (See Notes 3, 4 and 8 of the Notes to the Consolidated Financial Statements in our annual report to shareholders for the year ended December 31, 2015 for additional information on our investment strategies, hedging activities, and reinsurance, respectively.) As of June 30, 2016, Aflac Japan's SMR remains high and reflects a strong capital position.

Payments are made from Aflac Japan to the Parent Company for management fees and to Aflac U.S. for allocated expenses and remittances of earnings. The following table details Aflac Japan remittances for the six-month periods ended June 30.

#### Aflac Japan Remittances

| (In millions of dollars and billions of yen)              | 2016  | 2015  |
|---|-------|-------|
| Aflac Japan management fees paid to Parent Company        | \$ 31 | \$ 24 |
| Expenses allocated to Aflac Japan (in dollars)            | 57    | 54    |
| Aflac Japan profit remittances to Aflac U.S. (in dollars) | 219   | 250   |
| Aflac Japan profit remittances to Aflac U.S. (in yen)     | 25.0  | 30.0  |

We entered into foreign exchange forwards and options as part of an economic hedge on foreign exchange risk on 25.0 billion yen of profit repatriation received from Aflac Japan in February 2016, which reduced the amount of funds received by \$14 million when the yen were exchanged into dollars. In July 2016, Aflac Japan remitted profits to Aflac U.S. of 66.9 billion yen, or \$605 million. We had entered into foreign exchange forwards as part of a hedging strategy on 51.1 billion yen of the July 2016 repatriation, resulting in a \$33 million reduction of funds received when the yen were exchanged into dollars. Provided that capital conditions remain stable, we believe our financial strength in Japan positions us to repatriate in the range of 120.0 billion yen to 150.0 billion yen to the U.S. for the full year 2016.

For additional information on regulatory restrictions on dividends, profit repatriations and other transfers, see Note 13 of the Notes to the Consolidated Financial Statements and the Regulatory Restrictions subsection of MD&A, both in our annual report to shareholders for the year ended December 31, 2015.

Other

For information regarding commitments and contingent liabilities, see Note 11 of the Notes to the Consolidated Financial Statements.

### Item 3. Quantitative and Qualitative Disclosures about Market Risk

The information required by Item 3 is incorporated by reference from the Market Risks of Financial Instruments subsection of MD&A in Part I, Item 2 of this report.



#### Item 4. Controls and Procedures

##### Disclosure Controls and Procedures

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this quarterly report (the "Evaluation Date"). Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures are effective.

##### Changes in Internal Control Over Financial Reporting

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the second fiscal quarter of 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

## Issuer Purchases of Equity Securities

During the first six months of 2016, we repurchased shares of Aflac common stock as follows:

| Period                   | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>Per Share | Total<br>Number<br>of Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number of<br>Shares that<br>May Yet<br>Be<br>Purchased<br>Under the<br>Plans or<br>Programs |
|--------------------------|---|------------------------------------|--|--|
| January 1 - January 31   | 3,492,400                                 | \$ 57.29                           | 3,492,400  | 44,879,158   |
| February 1 - February 29 | 3,584,566                                 | 58.20                              | 3,435,930  | 41,443,228   |
| March 1 - March 31       | 3,229,684                                 | 62.07                              | 3,224,000  | 38,219,228   |
| April 1 - April 30       | 2,028,224                                 | 66.15                              | 2,026,445  | 36,192,783   |
| May 1 - May 31           | 1,929,098                                 | 68.97                              | 1,929,098  | 34,263,685   |
| June 1 - June 30         | 1,925,149                                 | 69.36                              | 1,918,479  | 32,345,206   |
| Total                    | 16,189,121 <sup>(2)</sup>                 | \$ 62.38                           | 16,026,352   | 32,345,206 <sup>(1)</sup>  |

<sup>(1)</sup>The total remaining shares available for purchase at June 30, 2016, consisted of 32,345,206 shares related to a 40,000,000 share repurchase authorization by the board of directors announced in 2015.

<sup>(2)</sup>During the first six months of 2016, 162,769 shares were purchased in connection with income tax withholding obligations related to the vesting of restricted-share-based awards during the period.



Item 6. Exhibits

(a) EXHIBIT INDEX

- 3.0 - Articles of Incorporation, as amended – incorporated by reference from Form 10-Q for June 30, 2008, Exhibit 3.0 (File No. 001-07434).
- 3.1 - Bylaws of the Corporation, as amended and restated – incorporated by reference from Form 8-K dated November 10, 2015, Exhibit 3.1 (File No. 001-07434).
- 4.0 - There are no instruments with respect to long-term debt not being registered in which the total amount of securities authorized exceeds 10% of the total assets of Aflac Incorporated and its subsidiaries on a consolidated basis. We agree to furnish a copy of any long-term debt instrument to the Securities and Exchange Commission upon request.
- 4.1 - Indenture, dated as of May 21, 2009, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee – incorporated by reference from Form 8-K dated May 21, 2009, Exhibit 4.1 (File No. 001-07434).
- 4.2 - First Supplemental Indenture, dated as of May 21, 2009, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 8.500% Senior Note due 2019) – incorporated by reference from Form 8-K dated May 21, 2009, Exhibit 4.2 (File No. 001-07434).
- 4.3 - Second Supplemental Indenture, dated as of December 17, 2009, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 6.900% Senior Note due 2039) – incorporated by reference from Form 8-K dated December 14, 2009, Exhibit 4.1 (File No. 001-07434).
- 4.4 - Third Supplemental Indenture, dated as of August 9, 2010, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 6.45% Senior Note due 2040) - incorporated by reference from Form 8-K dated August 4, 2010, Exhibit 4.1 (File No. 001-07434).
- 4.5 - Fourth Supplemental Indenture, dated as of August 9, 2010, between Aflac Incorporated and The Bank of New York and Mellon Trust Company, N.A., as trustee (including the form of 3.45% Senior Note due 2015) – incorporated by reference from Form 8-K dated August 4, 2010, Exhibit 4.2 (File No. 001-07434).
- 4.6 - Fifth Supplemental Indenture, dated as of February 10, 2012, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 2.65% Senior Note due 2017) - incorporated by reference from Form 8-K dated February 8, 2012, Exhibit 4.1 (File No. 001-07434).
- 4.7 - Sixth Supplemental Indenture, dated as of February 10, 2012, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 4.00% Senior Note due 2022) - incorporated by reference from Form 8-K dated February 8, 2012, Exhibit 4.2 (File No. 001-07434).
- 4.8 - Seventh Supplemental Indenture, dated as of July 31, 2012, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 2.65% Senior Note due 2017) - incorporated by reference from Form 8-K dated July 27, 2012, Exhibit 4.1 (File No. 001-07434).
- 4.9 - Eighth Supplemental Indenture, dated as of June 10, 2013, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 3.625% Senior Note due 2023) - incorporated by reference from Form 8-K dated June 10, 2013, Exhibit 4.1 (File No. 001-07434).
- 4.10 - Ninth Supplemental Indenture, dated as of November 7, 2014, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 3.625% Senior Note due 2024) - incorporated by reference from Form 8-K dated November 4, 2014, Exhibit 4.1 (File No. 001-07434).
- 4.11 -

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Tenth Supplemental Indenture, dated as of March 12, 2015, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 2.40% Senior Note due 2020) - incorporated by reference from Form 8-K dated March 9, 2015, Exhibit 4.1 (File No. 001-07434).

4.12 - Eleventh Supplemental Indenture, dated as of March 12, 2015, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 3.25% Senior Note due 2025) - incorporated by reference from Form 8-K dated March 9, 2015, Exhibit 4.2 (File No. 001-07434).

4.13 - Subordinated Indenture, dated as of September 26, 2012, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee - incorporated by reference from Form 8-K dated September 26, 2012, Exhibit 4.1 (File No. 001-07434).

- 4.14 - First Supplemental Indenture, dated as of September 26, 2012, between Aflac Incorporated and The Bank of New York Mellon Trust Company, N.A., as trustee (including the form of 5.50% Subordinated Debenture due 2052) - incorporated by reference from Form 8-K dated September 26, 2012, Exhibit 4.2 (File No. 001-07434).
- 10.0\* - American Family Corporation Retirement Plan for Senior Officers, as amended and restated October 1, 1989 – incorporated by reference from 1993 Form 10-K, Exhibit 10.2 (File No. 001-07434).
- 10.1\* - Amendment to American Family Corporation Retirement Plan for Senior Officers, dated December 8, 2008 – incorporated by reference from 2008 Form 10-K, Exhibit 10.1 (File No. 001-07434).
- 10.2\* - Aflac Incorporated Supplemental Executive Retirement Plan, as amended and restated January 1, 2009 – incorporated by reference from 2008 Form 10-K, Exhibit 10.5 (File No. 001-07434).
- 10.3\* - First Amendment to the Aflac Incorporated Supplemental Executive Retirement Plan, as amended and restated January 1, 2009 – incorporated by reference from 2012 Form 10-K, Exhibit 10.3 (File No. 001-07434).
- 10.4\* - Second Amendment to the Aflac Incorporated Supplemental Executive Retirement Plan, as amended and restated January 1, 2009 - incorporated by reference from 2014 Form 10-K, Exhibit 10.4 (File No. 001-07434).
- 10.5\* - Aflac Incorporated Executive Deferred Compensation Plan, as amended and restated, effective September 1, 2015 – incorporated by reference from Form 10-Q for September 30, 2015, Exhibit 10.5 (File No. 001-07434).
- 10.6\* - Aflac Incorporated 2013 Management Incentive Plan - incorporated by reference from the 2012 Proxy Statement, Appendix B (File No. 001-07434).
- 10.7\* - 1999 Aflac Associate Stock Bonus Plan, amended and restated as of January 1, 2013 - incorporated by reference from Form 10-Q for March 31, 2013, Exhibit 10.10 (File No. 001-07434).
- 10.8\* - Aflac Incorporated 1997 Stock Option Plan – incorporated by reference from the 1997 Shareholders’ Proxy Statement, Appendix B (File No. 001-07434).
- 10.9\* - Form of Officer Stock Option Agreement (Non-Qualifying Stock Option) under the Aflac Incorporated 1997 Stock Option Plan – incorporated by reference from Form 8-K dated January 28, 2005, Exhibit 10.5 (File No. 001-07434).
- 10.10\* - Form of Officer Stock Option Agreement (Incentive Stock Option) under the Aflac Incorporated 1997 Stock Option Plan – incorporated by reference from Form 8-K dated January 28, 2005, Exhibit 10.6 (File No. 001-07434).
- 10.11\* - Notice of grant of stock options and stock option agreement to officers under the Aflac Incorporated 1997 Stock Option Plan – incorporated by reference from Form 8-K dated January 28, 2005, Exhibit 10.7 (File No. 001-07434).
- 10.12\* - 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 – incorporated by reference from the 2012 Proxy Statement, Appendix A (File No. 001-07434).
- 10.13\* - Form of Non-Employee Director Stock Option Agreement (NQSO) under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.13 (File No. 001-07434).
- 10.14\* - Notice of grant of stock options to non-employee director under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.14 (File No. 001-07434).
- 10.15\* - Form of Non-Employee Director Restricted Stock Award Agreement under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.15 (File No. 001-07434).
- 10.16\* - Notice of restricted stock award to non-employee director under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.16 (File No. 001-07434).
- 10.17\* - U.S. Form of Employee Restricted Stock Award Agreement under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for

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March 31, 2016, Exhibit 10.17 (File No. 001-07434).

10.18\*- Japan Form of Employee Restricted Stock Award Agreement under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.18 (File No. 001-07434).

10.19\*- Notice of time based restricted stock award under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 – incorporated by reference from Form 10-Q for June 30, 2013, Exhibit 10.22 (File No. 001-07434).

10.20\*- Notice of performance based restricted stock award under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.20 (File No. 001-07434).

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- 10.21\* - U.S. Form of Employee Stock Option Agreement (Non-Qualifying Stock Option) under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.21 (File No. 001-07434).
- 10.22\* - Japan Form of Employee Stock Option Agreement (Non-Qualifying Stock Option) under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.22 (File No. 001-07434).
- 10.23\* - U.S. Form of Employee Stock Option Agreement (Incentive Stock Option) under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.23 (File No. 001-07434).
- 10.24\* - U.S. Notice of grant of stock options under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 – incorporated by reference from Form 10-Q for June 30, 2013, Exhibit 10.28 (File No. 001-07434).
- 10.25\* - Japan Notice of grant of stock options under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 – incorporated by reference from Form 10-Q for June 30, 2013, Exhibit 10.29 (File No. 001-07434).
- 10.26\* - Japan Form of Restricted Stock Unit Agreement under the 2004 Aflac Incorporated Long-Term Incentive Plan, as amended and restated March 14, 2012 - incorporated by reference from Form 10-Q for March 31, 2016, Exhibit 10.26 (File No. 001-07434).
- 10.27\* - Aflac Incorporated Retirement Plan for Directors Emeritus, as amended and restated, dated February 9, 2010 – incorporated by reference from 2009 Form 10-K, Exhibit 10.26 (File No. 001-07434).
- 10.28\* - Amendment to Aflac Incorporated Retirement Plan for Directors Emeritus, as amended and restated, dated August 10, 2010 – incorporated by reference from Form 10-Q for September 30, 2010, Exhibit 10.27 (File No. 001-07434).
- 10.29\* - Aflac Incorporated Employment Agreement with Daniel P. Amos, as amended and restated, dated August 20, 2015 - incorporated by reference from Form 10-Q for September 30, 2015, Exhibit 10.29 (File No. 001-07434).
- 10.30\* - Aflac Incorporated Employment Agreement with Kriss Cloninger III, as amended and restated, dated August 20, 2015 - incorporated by reference from Form 10-Q for September 30, 2015, Exhibit 10.30 (File No. 001-07434).
- 10.31\* - Aflac Employment Agreement with Paul S. Amos II, as amended and restated, dated August 19, 2015 - incorporated by reference from Form 10-Q for September 30, 2015, Exhibit 10.31 (File No. 001-07434).
- 10.32\* - Aflac Employment Agreement with Eric M. Kirsch, as amended and restated, dated December 1, 2015 - incorporated by reference from Form 8-K dated December 1, 2015, Exhibit 10.1 (File No. 001-07434).
- 10.33\* - Aflac Incorporated Employment Agreement with Frederick J. Crawford, effective June 30, 2015 – incorporated by reference from Form 8-K dated June 24, 2015, Exhibit 10.1 (File No. 001-07434).
- 11 - Statement regarding the computation of per-share earnings for the Registrant.
- 12 - Statement regarding the computation of ratio of earnings to fixed charges for the Registrant.
- 15 - Letter from KPMG LLP regarding unaudited interim financial information.
- 31.1 - Certification of CEO dated August 5, 2016, required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934.
- 31.2 - Certification of CFO dated August 5, 2016, required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934.
- 32 - Certification of CEO and CFO dated August 5, 2016, pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS - XBRL Instance Document.<sup>(1)</sup>
- 101.SCH - XBRL Taxonomy Extension Schema.
- 101.CAL - XBRL Taxonomy Extension Calculation Linkbase.
- 101.DEF - XBRL Taxonomy Extension Definition Linkbase.
- 101.LAB - XBRL Taxonomy Extension Label Linkbase.
- 101.PRE - XBRL Taxonomy Extension Presentation Linkbase.

Includes the following materials contained in this Quarterly Report on Form 10-Q for the period ended June 30, 2016, formatted in XBRL

(eXtensible Business Reporting Language):

- (i) Consolidated Statements of Earnings,
- (1) (ii) Consolidated Statements of Comprehensive Income (Loss),
- (iii) Consolidated Balance Sheets,
- (iv) Consolidated Statements of Shareholders' Equity,
- (v) Consolidated Statements of Cash Flows,
- (vi) Notes to the Consolidated Financial Statements

Management contract or compensatory plan or

- \* arrangement required to be filed as an exhibit pursuant to Item 6 of this report

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Aflac Incorporated

August 5, 2016 /s/ Frederick J. Crawford  
(Frederick J. Crawford)  
Executive Vice President,  
Chief Financial Officer

August 5, 2016 /s/ June Howard  
(June Howard)  
Senior Vice President, Financial Services; Chief Accounting Officer