

TRAVELERS COMPANIES, INC.

Form 10-Q

July 19, 2012

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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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## FORM 10-Q

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

For the quarterly period ended June 30, 2012

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: 001-10898

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# The Travelers Companies, Inc.

(Exact name of registrant as specified in its charter)

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**Minnesota**  
(State or other jurisdiction of  
incorporation or organization)

**41-0518860**  
(I.R.S. Employer  
Identification No.)

**485 Lexington Avenue**

**New York, NY 10017**

(Address of principal executive offices) (Zip Code)

**(917) 778-6000**

(Registrant's telephone number, including area code)

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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  Smaller reporting company   
(Do not check if a smaller reporting company)

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

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The number of shares of the Registrant's Common Stock, without par value, outstanding at July 16, 2012 was 385,358,110.

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**The Travelers Companies, Inc.**

**Quarterly Report on Form 10-Q**

**For Quarterly Period Ended June 30, 2012**

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF INCOME (LOSS) (Unaudited)**

(in millions, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenues</b>				
Premiums	\$ 5,529	\$ 5,503	\$ 11,052	\$ 10,874
Net investment income	738	758	1,478	1,537
Fee income	59	74	141	148
Net realized investment gains	4	19	14	39
Other revenues	29	34	66	68
<b>Total revenues</b>	<b>6,359</b>	<b>6,388</b>	<b>12,751</b>	<b>12,666</b>
<b>Claims and expenses</b>				
Claims and claim adjustment expenses	3,786	5,141	7,150	8,523
Amortization of deferred acquisition costs	976	970	1,947	1,918
General and administrative expenses	893	907	1,777	1,790
Interest expense	96	97	192	193
<b>Total claims and expenses</b>	<b>5,751</b>	<b>7,115</b>	<b>11,066</b>	<b>12,424</b>
<b>Income (loss) before income taxes</b>	<b>608</b>	<b>(727)</b>	<b>1,685</b>	<b>242</b>
Income tax expense (benefit)	109	(363)	380	(233)
<b>Net income (loss)</b>	<b>\$ 499</b>	<b>\$ (364)</b>	<b>\$ 1,305</b>	<b>\$ 475</b>
<b>Net income (loss) per share</b>				
Basic	\$ 1.27	\$ (0.88)	\$ 3.32	\$ 1.11
Diluted	\$ 1.26	\$ (0.88)	\$ 3.29	\$ 1.10
<b>Weighted average number of common shares outstanding</b>				
Basic	388.0	418.6	390.0	423.3
Diluted	391.6	418.6	393.5	429.1

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	Three Months Ended		Six Months Ended	
	2012	June 30, 2011	2012	June 30, 2011
<b>Net Realized Investment Gains</b>				
Other-than-temporary impairment losses:				
Total gains	\$ 11	\$ 5	\$ 11	\$ 7
Non-credit component of impairments recognized in accumulated other comprehensive income	(15)	(9)	(19)	(15)
Other-than-temporary impairment losses	(4)	(4)	(8)	(8)
Other net realized investment gains	8	23	22	47
<b>Net realized investment gains</b>	<b>\$ 4</b>	<b>\$ 19</b>	<b>\$ 14</b>	<b>\$ 39</b>

See notes to consolidated financial statements (unaudited).

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (Unaudited)**

(in millions)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Net income (loss)</b>	\$ 499	\$ (364)	\$ 1,305	\$ 475
<b>Other comprehensive income:</b>				
Change in net unrealized gains on investment securities:				
Having no credit losses recognized in the consolidated statement of income	216	645	139	539
Having credit losses recognized in the consolidated statement of income	5	(10)	30	18
Net changes in benefit plan assets and obligations	22	19	42	37
Net changes in unrealized foreign currency translation and other changes	(86)	16	(22)	86
<b>Other comprehensive income before income taxes</b>	<b>157</b>	<b>670</b>	<b>189</b>	<b>680</b>
Income tax expense	66	231	64	224
<b>Other comprehensive income, net of taxes</b>	<b>91</b>	<b>439</b>	<b>125</b>	<b>456</b>
<b>Comprehensive income</b>	<b>\$ 590</b>	<b>\$ 75</b>	<b>\$ 1,430</b>	<b>\$ 931</b>

See notes to consolidated financial statements (unaudited).



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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEET

(in millions)

	June 30, 2012	December 31, 2011
<b>Assets</b>		
Fixed maturities, available for sale, at fair value (amortized cost \$60,313 and \$59,994)	\$ 64,705	\$ 64,232
Equity securities, available for sale, at fair value (cost \$436 and \$414)	595	559
Real estate investments	899	865
Short-term securities	3,275	3,594
Other investments	3,470	3,451
<b>Total investments</b>	<b>72,944</b>	<b>72,701</b>
Cash	230	214
Investment income accrued	751	768
Premiums receivable	6,197	5,730
Reinsurance recoverables	10,404	11,155
Ceded unearned premiums	874	828
Deferred acquisition costs	1,839	1,786
Deferred taxes		7
Contractholder receivables	4,903	5,186
Goodwill	3,365	3,365
Other intangible assets	405	433
Other assets	2,418	2,402
<b>Total assets</b>	<b>\$ 104,330</b>	<b>\$ 104,575</b>
<b>Liabilities</b>		
Claims and claim adjustment expense reserves	\$ 50,793	\$ 51,392
Unearned premium reserves	11,449	11,102
Contractholder payables	4,903	5,186
Payables for reinsurance premiums	413	389
Deferred taxes	194	
Debt	6,349	6,605
Other liabilities	5,180	5,424
<b>Total liabilities</b>	<b>79,281</b>	<b>80,098</b>
<b>Shareholders equity</b>		
Common stock (1,750.0 shares authorized; 386.0 and 392.8 shares issued and outstanding)	20,970	20,732
Retained earnings	20,541	19,579
Accumulated other comprehensive income	2,130	2,005
Treasury stock, at cost (361.4 and 349.0 shares)	(18,592)	(17,839)
<b>Total shareholders equity</b>	<b>25,049</b>	<b>24,477</b>
<b>Total liabilities and shareholders equity</b>	<b>\$ 104,330</b>	<b>\$ 104,575</b>

See notes to consolidated financial statements (unaudited).

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)**

(in millions)

For the six months ended June 30,	2012	2011
<b>Convertible preferred stock savings plan</b>		
Balance, beginning of year	\$	\$ 68
Redemptions during period		(5)
Conversion to common stock		(63)
Balance, end of period		
<b>Common stock</b>		
Balance, beginning of year	20,732	20,162
Employee share-based compensation	149	263
Common shares issued conversion of preferred stock		93
Compensation amortization under share-based plans and other changes	89	89
Balance, end of period	20,970	20,607
<b>Retained earnings</b>		
Balance, beginning of year	19,579	18,847
Net income	1,305	475
Dividends	(343)	(331)
Premium on preferred stock converted to common stock		(30)
Other		5
Balance, end of period	20,541	18,966
<b>Accumulated other comprehensive income, net of tax</b>		
Balance, beginning of year	2,005	1,255
Other comprehensive income	125	456
Balance, end of period	2,130	1,711
<b>Treasury stock (at cost)</b>		
Balance, beginning of year	(17,839)	(14,857)
Treasury shares acquired share repurchase authorization	(700)	(1,337)
Net shares acquired related to employee share-based compensation plans	(53)	(82)
Balance, end of period	(18,592)	(16,276)
Total common shareholders' equity	25,049	25,008
Total shareholders' equity	\$ 25,049	\$ 25,008
<b>Common shares outstanding</b>		
Balance, beginning of year	392.8	434.6
Treasury shares acquired share repurchase authorization	(11.6)	(22.8)
Common shares issued conversion of preferred stock		1.5
Net shares issued under employee share-based compensation plans	4.8	6.2

Balance, end of period	386.0	419.5
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See notes to consolidated financial statements (unaudited).

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)**

(in millions)

For the six months ended June 30,	2012	2011
<b>Cash flows from operating activities</b>		
Net income	\$ 1,305	\$ 475
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized investment gains	(14)	(39)
Depreciation and amortization	412	405
Deferred federal income tax expense	125	137
Amortization of deferred acquisition costs	1,947	1,918
Equity in income from other investments	(228)	(231)
Premiums receivable	(468)	(542)
Reinsurance recoverables	752	225
Deferred acquisition costs	(2,000)	(1,973)
Claims and claim adjustment expense reserves	(599)	889
Unearned premium reserves	346	395
Other	(313)	(758)
<b>Net cash provided by operating activities</b>	<b>1,265</b>	<b>901</b>
<b>Cash flows from investing activities</b>		
Proceeds from maturities of fixed maturities	4,167	3,234
Proceeds from sales of investments:		
Fixed maturities	542	736
Equity securities	22	47
Real estate investments	3	
Other investments	386	285
Purchases of investments:		
Fixed maturities	(5,200)	(3,547)
Equity securities	(33)	(103)
Real estate investments	(58)	(35)
Other investments	(221)	(629)
Net sales of short-term securities	367	597
Securities transactions in course of settlement	77	213
Other	(133)	(143)
<b>Net cash provided by (used in) investing activities</b>	<b>(81)</b>	<b>655</b>
<b>Cash flows from financing activities</b>		
Payment of debt	(258)	(8)
Dividends paid to shareholders	(341)	(329)
Issuance of common stock employee share options	170	245
Treasury stock acquired share repurchase authorization	(707)	(1,360)
Treasury stock acquired net employee share-based compensation	(52)	(46)
Excess tax benefits from share-based payment arrangements	19	11
<b>Net cash used in financing activities</b>	<b>(1,169)</b>	<b>(1,487)</b>
Effect of exchange rate changes on cash	1	4

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Net increase in cash		<b>16</b>		73
Cash at beginning of year		<b>214</b>		200
<b>Cash at end of period</b>		<b>\$ 230</b>	<b>\$</b>	273
<b>Supplemental disclosure of cash flow information</b>				
Income taxes paid		<b>\$ 296</b>	<b>\$</b>	291
Interest paid		<b>\$ 191</b>	<b>\$</b>	191

See notes to consolidated financial statements (unaudited).

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

**1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES**

**Basis of Presentation**

The interim consolidated financial statements include the accounts of The Travelers Companies, Inc. (together with its subsidiaries, the Company). These financial statements are prepared in conformity with U.S. generally accepted accounting principles (GAAP) and are unaudited. In the opinion of the Company's management, all adjustments necessary for a fair presentation have been reflected. Certain financial information that is normally included in annual financial statements prepared in accordance with GAAP, but that is not required for interim reporting purposes, has been omitted. All material intercompany transactions and balances have been eliminated. Certain reclassifications have been made to the 2011 consolidated financial statements and notes to conform to the 2012 presentation. The accompanying interim consolidated financial statements and related notes should be read in conjunction with the Company's consolidated financial statements and related notes included in the Company's 2011 Annual Report on Form 10-K.

The preparation of the interim consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the interim consolidated financial statements and the reported amounts of revenues and claims and expenses during the reporting period. Actual results could differ from those estimates.

**Adoption of Accounting Standards Updates**

*Presentation of Comprehensive Income*

In June 2011, the Financial Accounting Standards Board (FASB) issued updated guidance to increase the prominence of items reported in other comprehensive income by eliminating the option of presenting components of comprehensive income as part of the statement of changes in shareholders' equity. The updated guidance requires that all nonowner changes in shareholders' equity be presented either as a single continuous statement of comprehensive income or in two separate but consecutive statements.

The updated guidance was effective for the quarter ended March 31, 2012 and was applied retrospectively. The Company's adoption of this guidance resulted in a change in the presentation of the Company's consolidated financial statements but did not have any effect on the Company's results of operations, financial position or liquidity.

*Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts*

In October 2010, the FASB issued updated guidance to address diversity in practice for the accounting for costs associated with acquiring or renewing insurance contracts. This guidance modifies the definition of acquisition costs to specify that a cost must be directly related to the successful acquisition of a new or renewal insurance contract in order to be deferred. If application of this guidance would result in the capitalization of acquisition costs that had not previously been capitalized by a reporting entity, the entity may elect not to capitalize those costs.

The updated guidance was effective for the quarter ended March 31, 2012. The adoption of this guidance did not have any effect on the Company's results of operations, financial position or liquidity.

*Transfers and Servicing*

In April 2011, the FASB issued updated guidance related to the accounting for repurchase agreements and other agreements that entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The updated guidance eliminates the criteria to assess whether a transferor is required to have the ability to repurchase or redeem the financial assets in order to demonstrate effective control over the transferred asset. Transferors that maintain effective control over a transferred asset are required to account for the transaction as a secured borrowing rather than a sale.

The updated guidance was effective for the quarter ended March 31, 2012. The updated guidance applies to transactions or modifications of existing transactions that occur on or after the effective date. The adoption of this guidance did not have any effect on the Company's results of operations, financial position or liquidity.



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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), (Continued)**

**1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES, Continued**

*Intangibles - Goodwill and Other*

In September 2011, the FASB issued updated guidance that modifies the manner in which the two-step impairment test of goodwill is applied. Under the updated guidance, an entity may assess qualitative factors (such as changes in management, key personnel, strategy, key technology or customers) that may impact a reporting unit's fair value and lead to the determination that it is more likely than not that the fair value of a reporting unit is less than its carrying value, including goodwill. If an entity determines that it is more likely than not, it must perform an impairment test.

The first step of the impairment test involves comparing the estimated fair value of a reporting unit to its carrying value, including goodwill. If the carrying value of a reporting unit exceeds the estimated fair value, a second step must be performed to measure the amount of goodwill impairment, if any. In the second step, the implied fair value of the reporting unit's goodwill is determined in the same manner as goodwill is measured in a business combination (i.e., by measuring the fair value of the reporting unit's assets, liabilities and unrecognized intangible assets and determining the remaining amount ascribed to goodwill) and comparing the amount of the implied goodwill to the carrying amount of the goodwill. If the carrying value of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to the excess.

The updated guidance was effective for the quarter ended March 31, 2012. The adoption of this guidance did not have any effect on the Company's results of operations, financial position or liquidity.

**Nature of Operations**

The Company is organized into three reportable business segments: Business Insurance; Financial, Professional & International Insurance; and Personal Insurance. These segments reflect the manner in which the Company's businesses are currently managed and represent an aggregation of products and services based on type of customer, how the business is marketed and the manner in which risks are underwritten. The specific business segments are as follows:

**Business Insurance**

The Business Insurance segment offers a broad array of property and casualty insurance and insurance-related services to its clients primarily in the United States. Business Insurance is organized into the following six groups, which collectively comprise Business Insurance Core operations: Select Accounts; Commercial Accounts; National Accounts; Industry-Focused Underwriting; Target Risk Underwriting; and Specialized Distribution.

Business Insurance also includes the Special Liability Group (which manages the Company's asbestos and environmental liabilities) and the assumed reinsurance and certain international and other runoff operations, which collectively are referred to as Business Insurance Other.

### **Financial, Professional & International Insurance**

The Financial, Professional & International Insurance segment includes surety and financial liability coverages, which primarily use credit-based underwriting processes, as well as property and casualty products that are primarily marketed on a domestic basis in the United Kingdom, Canada and the Republic of Ireland, and on an international basis through Lloyd's. The segment includes Bond & Financial Products as well as International.

### **Personal Insurance**

The Personal Insurance segment writes a broad range of property and casualty insurance covering individuals' personal risks. The primary products of automobile and homeowners insurance are complemented by a broad suite of related coverages.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), (Continued)

## 2. SEGMENT INFORMATION

The following tables summarize the components of the Company's revenues, operating income (loss) and total assets by reportable business segments:

(for the three months ended June 30, in millions)	Business Insurance	Financial, Professional & International Insurance	Personal Insurance	Total Reportable Segments
<b>2012</b>				
Premiums	\$ 2,860	\$ 766	\$ 1,903	\$ 5,529
Net investment income	536	99	103	738
Fee income	58	1		59
Other revenues	8	5	16	29
Total operating revenues (1)	\$ 3,462	\$ 871	\$ 2,022	\$ 6,355
Operating income (1)	\$ 362	\$ 182	\$ 17	\$ 561
<b>2011</b>				
Premiums	\$ 2,802	\$ 810	\$ 1,891	\$ 5,503
Net investment income	541	105	112	758
Fee income	74			74
Other revenues	10	6	18	34
Total operating revenues (1)	\$ 3,427	\$ 921	\$ 2,021	\$ 6,369
Operating income (loss) (1)	\$ 11	\$ 164	\$ (471)	\$ (296)

(1) Operating revenues for reportable business segments exclude net realized investment gains (losses). Operating income (loss) for reportable business segments equals net income (loss) excluding the after-tax impact of net realized investment gains (losses).

(for the six months ended June 30, in millions)	Business Insurance	Financial, Professional & International Insurance	Personal Insurance	Total Reportable Segments
<b>2012</b>				
Premiums	\$ 5,736	\$ 1,503	\$ 3,813	\$ 11,052
Net investment income	1,068	203	207	1,478

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Fee income		<b>140</b>		<b>1</b>		<b>141</b>
Other revenues		<b>22</b>		<b>13</b>	<b>35</b>	<b>70</b>
Total operating revenues (1)	\$	<b>6,966</b>	\$	<b>1,720</b>	\$	<b>4,055</b>
Operating income (1)	\$	<b>974</b>	\$	<b>331</b>	\$	<b>125</b>
<b>2011</b>						
Premiums	\$	5,547	\$	1,583	\$	3,744
Net investment income		1,097		211		229
Fee income		148				148
Other revenues		19		13		36
Total operating revenues (1)	\$	6,811	\$	1,807	\$	4,009
Operating income (loss) (1)	\$	615	\$	284	\$	(301)

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(1) Operating revenues for reportable business segments exclude net realized investment gains (losses). Operating income (loss) for reportable business segments equals net income (loss) excluding the after-tax impact of net realized investment gains (losses).

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 2. SEGMENT INFORMATION, Continued

## Business Segment Reconciliations

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenue reconciliation</b>				
Earned premiums				
Business Insurance:				
Workers compensation	\$ 754	\$ 712	\$ 1,537	\$ 1,392
Commercial automobile	488	480	974	953
Property	401	401	793	802
General liability	437	429	869	857
Commercial multi-peril	773	778	1,548	1,540
Other	7	2	15	3
Total Business Insurance	2,860	2,802	5,736	5,547
Financial, Professional & International Insurance:				
Fidelity and surety	236	249	459	483
General liability	210	211	417	415
International	278	311	544	609
Other	42	39	83	76
Total Financial, Professional & International Insurance	766	810	1,503	1,583
Personal Insurance:				
Automobile	918	931	1,846	1,846
Homeowners and other	985	960	1,967	1,898
Total Personal Insurance	1,903	1,891	3,813	3,744
Total earned premiums	5,529	5,503	11,052	10,874
Net investment income	738	758	1,478	1,537
Fee income	59	74	141	148
Other revenues	29	34	70	68
Total operating revenues for reportable segments	6,355	6,369	12,741	12,627
Other revenues			(4)	
Net realized investment gains	4	19	14	39

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Total consolidated revenues	\$	<b>6,359</b>	\$	6,388	\$	<b>12,751</b>	\$	12,666
<b>Income reconciliation, net of tax</b>								
Total operating income (loss) for reportable segments	\$	<b>561</b>	\$	(296)	\$	<b>1,430</b>	\$	598
Interest Expense and Other (1)		<b>(66)</b>		(81)		<b>(134)</b>		(149)
Total operating income (loss)		<b>495</b>		(377)		<b>1,296</b>		449
Net realized investment gains		<b>4</b>		13		<b>9</b>		26
Total consolidated net income (loss)	\$	<b>499</b>	\$	(364)	\$	<b>1,305</b>	\$	475

(1) The primary component of Interest Expense and Other is after-tax interest expense of \$63 million in each of the three months ended June 30, 2012 and 2011, and \$125 million in each of the six months ended June 30, 2012 and 2011.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****2. SEGMENT INFORMATION, Continued**

(in millions)	June 30, 2012	December 31, 2011
<b>Asset reconciliation:</b>		
Business Insurance	\$ 76,968	\$ 76,909
Financial, Professional & International Insurance	13,491	13,355
Personal Insurance	13,527	13,614
Total assets for reportable segments	103,986	103,878
Other assets (1)	344	697
Total consolidated assets	\$ 104,330	\$ 104,575

(1) The primary components of other assets at both dates were other intangible assets. The December 31, 2011 total also included deferred taxes.

**3. INVESTMENTS****Fixed Maturities**

The amortized cost and fair value of investments in fixed maturities classified as available for sale were as follows:

(at June 30, 2012, in millions)	Amortized Cost	Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,072	\$ 85	\$	\$ 2,157
Obligations of states, municipalities and political subdivisions:				
Pre-refunded	7,720	585		8,305
All other	28,430	2,231	15	30,646

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Total obligations of states, municipalities and political subdivisions	36,150	2,816	15	38,951
Debt securities issued by foreign governments	2,250	85	1	2,334
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	3,075	250	7	3,318
All other corporate bonds	16,740	1,207	33	17,914
Redeemable preferred stock	26	5		31
Total	\$ 60,313	\$ 4,448	\$ 56	\$ 64,705

(at December 31, 2011, in millions)	Amortized Cost	Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,396	\$ 101	\$	\$ 2,497
Obligations of states, municipalities and political subdivisions:				
Pre-refunded	6,820	513	1	7,332
All other	29,391	2,303	4	31,690
Total obligations of states, municipalities and political subdivisions	36,211	2,816	5	39,022
Debt securities issued by foreign governments	2,228	91	1	2,318
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	3,288	249	22	3,515
All other corporate bonds	15,845	1,066	61	16,850
Redeemable preferred stock	26	4		30
Total	\$ 59,994	\$ 4,327	\$ 89	\$ 64,232



Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****3. INVESTMENTS, Continued**

Pre-refunded bonds of \$8.31 billion and \$7.33 billion at June 30, 2012 and December 31, 2011, respectively, were bonds for which an irrevocable trust has been established to fund the remaining payments of principal and interest.

**Equity Securities**

The cost and fair value of investments in equity securities were as follows:

(at June 30, 2012, in millions)	Cost	Gains	Gross Unrealized Losses	Fair Value
Common stock	\$ 340	\$ 130	\$ 3	\$ 467
Non-redeemable preferred stock	96	33	1	128
Total	\$ 436	\$ 163	\$ 4	\$ 595

(at December 31, 2011, in millions)	Cost	Gains	Gross Unrealized Losses	Fair Value
Common stock	\$ 311	\$ 120	\$ 3	\$ 428
Non-redeemable preferred stock	103	29	1	131
Total	\$ 414	\$ 149	\$ 4	\$ 559

**Unrealized Investment Losses**

The following tables summarize, for all investments in an unrealized loss position at June 30, 2012 and December 31, 2011, the aggregate fair value and gross unrealized loss by length of time those securities have been continuously in an unrealized loss position.

(at June 30, 2012, in millions)	Less than 12 months Fair Value	Gross Unrealized	12 months or longer Fair Value	Gross Unrealized	Fair Value	Total Gross Unrealized
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	Losses		Losses		Losses	
<b>Fixed maturities</b>						
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$	919	\$	\$	\$	919
Obligations of states, municipalities and political subdivisions		1,286		12		30
Debt securities issued by foreign governments		151		1		151
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities		70		1		145
All other corporate bonds		803		16		17
						6
						215
						940
						33
Total fixed maturities		3,229		30		312
						26
						3,541
						56
<b>Equity securities</b>						
Common stock		56		2		4
Non-redeemable preferred stock		34		1		5
						1
						60
						3
Total equity securities		90		3		9
						1
						99
						4
Total	\$	3,319	\$	33	\$	321
						27
						3,640
						60

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 3. INVESTMENTS, Continued

(at December 31, 2011, in millions)	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>Fixed maturities</b>						
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 356	\$	\$	\$	\$ 356	\$
Obligations of states, municipalities and political subdivisions	27		191	5	218	5
Debt securities issued by foreign governments	96	1	2		98	1
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	362	12	155	10	517	22
All other corporate bonds	1,295	42	105	19	1,400	61
<b>Total fixed maturities</b>	<b>2,136</b>	<b>55</b>	<b>453</b>	<b>34</b>	<b>2,589</b>	<b>89</b>
<b>Equity securities</b>						
Common stock	64	3			64	3
Non-redeemable preferred stock	37	1	7		44	1
<b>Total equity securities</b>	<b>101</b>	<b>4</b>	<b>7</b>		<b>108</b>	<b>4</b>
<b>Total</b>	<b>\$ 2,237</b>	<b>\$ 59</b>	<b>\$ 460</b>	<b>\$ 34</b>	<b>\$ 2,697</b>	<b>\$ 93</b>

The following table summarizes, for all fixed maturities and equity securities reported at fair value for which fair value is less than 80% of amortized cost at June 30, 2012, the gross unrealized investment loss by length of time those securities have continuously been in an unrealized loss position of greater than 20% of amortized cost:

(in millions)	Period For Which Fair Value Is Less Than 80% of Amortized Cost				Total
	3 Months or Less	Greater Than 3 Months, 6 Months or Less	Greater Than 6 Months, 12 Months or Less	Greater Than 12 Months	
<b>Fixed maturities</b>					
Mortgage-backed securities	\$	\$	\$	\$	\$
Other	2			9	11
<b>Total fixed maturities</b>	<b>2</b>			<b>9</b>	<b>11</b>

Equity securities

<b>Total</b>	<b>\$</b>	<b>2</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>9</b>	<b>\$</b>	<b>11</b>
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Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****3. INVESTMENTS, Continued****Impairment Charges**

Impairment charges included in net realized investment gains in the consolidated statement of income (loss) were as follows:

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Fixed maturities</b>				
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$	\$	\$	\$
Obligations of states, municipalities and political subdivisions				
Debt securities issued by foreign governments				
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	2	2	3	4
All other corporate bonds	1	1	3	3
Redeemable preferred stock				
<b>Total fixed maturities</b>	<b>3</b>	<b>3</b>	<b>6</b>	<b>7</b>
<b>Equity securities</b>				
Common stock		1		1
Non-redeemable preferred stock				
<b>Total equity securities</b>		<b>1</b>		<b>1</b>
<b>Other investments</b>	<b>1</b>		<b>2</b>	
<b>Total</b>	<b>\$ 4</b>	<b>\$ 4</b>	<b>\$ 8</b>	<b>\$ 8</b>

The following tables present the changes during the reporting period in the credit component of other-than-temporary impairments (OTTI) on fixed maturities recognized in the consolidated statement of income (loss) for which a portion of the OTTI was recognized in other comprehensive income:



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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 3. INVESTMENTS, Continued

(for the three months ended June 30, in millions)	2012					
	Cumulative OTTI Credit Losses Recognized for Securities Held, Beginning of Period	Additions for OTTI Securities Where No Credit Losses Were Previously Recognized	Additions for OTTI Securities Where Credit Losses Have Been Previously Recognized	Reductions Due to Sales/Defaults of Credit-Impaired Securities	Adjustments to Book Value of Credit-Impaired Securities due to Changes in Cash Flows	Cumulative OTTI Credit Losses Recognized for Securities Still Held, End of Period
<b>Fixed maturities</b>						
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	\$ 59	\$	\$ 2	\$	\$	\$ 61
All other corporate bonds	97		1		1	99
<b>Total fixed maturities</b>	<b>\$ 156</b>	<b>\$</b>	<b>\$ 3</b>	<b>\$</b>	<b>\$ 1</b>	<b>\$ 160</b>

(for the six months ended June 30, in millions)

<b>Fixed maturities</b>						
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	\$ 58	\$	\$ 3	\$	\$	\$ 61
All other corporate bonds	94		3		2	99
<b>Total fixed maturities</b>	<b>\$ 152</b>	<b>\$</b>	<b>\$ 6</b>	<b>\$</b>	<b>\$ 2</b>	<b>\$ 160</b>

(for the three months ended June 30, in millions)	2011					
	Cumulative OTTI Credit Losses Recognized for Securities Held, Beginning of Period	Additions for OTTI Securities Where No Credit Losses Were Previously Recognized	Additions for OTTI Securities Where Credit Losses Have Been Previously Recognized	Reductions Due to Sales/Defaults of Credit-Impaired Securities	Adjustments to Book Value of Credit-Impaired Securities due to Changes in Cash Flows	Cumulative OTTI Credit Losses Recognized for Securities Still Held, End of Period
<b>Fixed maturities</b>						
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	\$ 49	\$	\$ 2	\$	\$	\$ 51
All other corporate bonds	90		1		1	92

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Total fixed maturities	\$	139	\$		\$	3	\$		\$	1	\$	143
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(for the six months ended June 30, in millions)

**Fixed maturities**

Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	\$	47	\$		\$	4	\$		\$		\$	51
All other corporate bonds		88		1		2		(1)		2		92
Total fixed maturities	\$	135	\$	1	\$	6	\$	(1)	\$	2	\$	143



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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**4. FAIR VALUE MEASUREMENTS**

The Company's estimates of fair value for financial assets and financial liabilities are based on the framework established in the fair value accounting guidance. The framework is based on the inputs used in valuation, gives the highest priority to quoted prices in active markets and requires that observable inputs be used in the valuations when available. The disclosure of fair value estimates in the fair value accounting guidance hierarchy is based on whether the significant inputs into the valuation are observable. In determining the level of the hierarchy in which the estimate is disclosed, the highest priority is given to unadjusted quoted prices in active markets and the lowest priority to unobservable inputs that reflect the Company's significant market assumptions. The level in the fair value hierarchy within which the fair value measurement is reported is based on the lowest level input that is significant to the measurement in its entirety. The three levels of the hierarchy are as follows:

- Level 1 - Unadjusted quoted market prices for identical assets or liabilities in active markets that the Company has the ability to access.
  
- Level 2 - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; or valuations based on models where the significant inputs are observable (e.g., interest rates, yield curves, prepayment speeds, default rates, loss severities, etc.) or can be corroborated by observable market data.
  
- Level 3 - Valuations based on models where significant inputs are not observable. The unobservable inputs reflect the Company's own assumptions about the inputs that market participants would use.

*Valuation of Investments Reported at Fair Value in Financial Statements*

The fair value of a financial instrument is the estimated amount at which the instrument could be exchanged in an orderly transaction between knowledgeable, unrelated, willing parties, i.e., not in a forced transaction. The estimated fair value of a financial instrument may differ from the amount that could be realized if the security was sold in an immediate sale, e.g., a forced transaction. Additionally, the valuation of investments is more subjective when markets are less liquid due to the lack of market based inputs, which may increase the potential that the estimated fair value of an investment is not reflective of the price at which an actual transaction would occur.

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For investments that have quoted market prices in active markets, the Company uses the unadjusted quoted market prices as fair value and includes these prices in the amounts disclosed in Level 1 of the hierarchy. The Company receives the quoted market prices from a third party, nationally recognized pricing service (pricing service). When quoted market prices are unavailable, the Company utilizes a pricing service to determine an estimate of fair value, which is mainly used for its fixed maturity investments. The fair value estimates provided from this pricing service are included in the amount disclosed in Level 2 of the hierarchy. If quoted market prices and an estimate from a pricing service are unavailable, the Company produces an estimate of fair value based on internally developed valuation techniques, which, depending on the level of observable market inputs, will render the fair value estimate as Level 2 or Level 3. The Company bases all of its estimates of fair value for assets on the bid price as it represents what a third-party market participant would be willing to pay in an arm's length transaction.

### *Fixed Maturities*

The Company utilizes a pricing service to estimate fair value measurements for approximately 98% of its fixed maturities. The pricing service utilizes market quotations for fixed maturity securities that have quoted prices in active markets. Since fixed maturities other than U.S. Treasury securities generally do not trade on a daily basis, the pricing service prepares estimates of fair value measurements for these securities using its proprietary pricing applications, which include available relevant market information, benchmark curves, benchmarking of like securities, sector groupings and matrix pricing. Additionally, the pricing service uses an Option Adjusted Spread model to develop prepayment and interest rate scenarios.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**4. FAIR VALUE MEASUREMENTS, Continued**

The pricing service evaluates each asset class based on relevant market information, relevant credit information, perceived market movements and sector news. The market inputs utilized in the pricing evaluation, listed in the approximate order of priority, include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data, and industry and economic events. The extent of the use of each market input depends on the asset class and the market conditions. Depending on the security, the priority of the use of inputs may change or some market inputs may not be relevant. For some securities, additional inputs may be necessary.

The pricing service utilized by the Company has indicated that they will only produce an estimate of fair value if there is objectively verifiable information to produce a valuation. If the pricing service discontinues pricing an investment, the Company would be required to produce an estimate of fair value using some of the same methodologies as the pricing service but would have to make assumptions for market-based inputs that are unavailable due to market conditions.

The fair value estimates of most fixed maturity investments are based on observable market information rather than market quotes. Accordingly, the estimates of fair value for such fixed maturities, other than U.S. Treasury securities, provided by the pricing service are included in the amount disclosed in Level 2 of the hierarchy. The estimated fair value of U.S. Treasury securities is included in the amount disclosed in Level 1 as the estimates are based on unadjusted market prices.

The Company also holds certain fixed maturity investments which are not priced by the pricing service and, accordingly, estimates the fair value of such fixed maturities using an internal matrix that is based on market information regarding interest rates, credit spreads and liquidity. The underlying source data for calculating the matrix of credit spreads relative to the U.S. Treasury curve are the BofA Merrill Lynch U.S. Corporate Index and the BofA Merrill Lynch High Yield BB Rated Index. The Company includes the fair value estimates of these corporate bonds in Level 2, since all significant inputs are market observable.

While the vast majority of the Company's municipal bonds and corporate bonds are included in Level 2, the Company holds a number of municipal bonds and corporate bonds which are not valued by the pricing service and estimates the fair value of these bonds using an internal pricing matrix with some unobservable inputs that are significant to the valuation. Due to the limited amount of observable market information, the Company includes the fair value estimates for these particular bonds in Level 3. The fair value of the fixed maturities for which the Company used an internal pricing matrix was \$103 million and \$88 million at June 30, 2012 and December 31, 2011, respectively. Additionally, the Company holds a small amount of other fixed maturity investments that have characteristics that make them unsuitable for matrix pricing. For these fixed maturities, the Company obtains a quote from a broker (primarily the market maker). The fair value of the fixed maturities for which the Company received a broker quote was \$151 million and \$162 million at June 30, 2012 and December 31, 2011, respectively. Due to the disclaimers on the quotes that indicate that the price is indicative only, the Company includes these fair value estimates in Level 3.

*Equities Public Common and Preferred*

For public common and preferred stocks, the Company receives prices from a nationally recognized pricing service that are based on observable market transactions and includes these estimates in the amount disclosed in Level 1. Infrequently, current market quotes in active markets are unavailable for certain non-redeemable preferred stocks held by the Company. In these instances, the Company receives an estimate of fair value from the pricing service that provides fair value estimates for the Company's fixed maturities. The service utilizes some of the same methodologies to price the non-redeemable preferred stocks as it does for the fixed maturities. The Company includes the fair value estimate for these non-redeemable preferred stocks in the amount disclosed in Level 2.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****4. FAIR VALUE MEASUREMENTS, Continued***Other Investments*

The Company holds investments in various publicly-traded securities which are reported in other investments. These investments include securities in the Company's trading portfolio, mutual funds and other small holdings. The \$42 million fair value of these investments at both June 30, 2012 and December 31, 2011 was disclosed in Level 1. At June 30, 2012 and December 31, 2011, the Company held investments in non-public common and preferred equity securities, with fair value estimates of \$44 million at both dates reported in other investments, where the fair value estimate is determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth and other business and market sector fundamentals. Due to the significant unobservable inputs in these valuations, the Company includes the total fair value estimate for all of these investments at June 30, 2012 and December 31, 2011 in the amount disclosed in Level 3.

*Derivatives*

At both June 30, 2012 and December 31, 2011, the Company held \$22 million of convertible bonds containing embedded conversion options that are valued separately from the host bond contract in the amount disclosed in Level 2 fixed maturities.

*Fair Value Hierarchy*

The following tables present the level within the fair value hierarchy at which the Company's financial assets and financial liabilities reported at fair value are measured on a recurring basis at June 30, 2012 and December 31, 2011. An investment transferred between levels during a period is transferred at its fair value as of the beginning of that period.

(at June 30, 2012, in millions)	Total	Level 1	Level 2	Level 3
<b>Invested assets:</b>				
<b>Fixed maturities</b>				
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,157	\$ 2,137	\$ 20	

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Obligations of states, municipalities and political subdivisions	38,951		38,922	29
Debt securities issued by foreign governments	2,334		2,334	
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	3,318		3,313	5
All other corporate bonds	17,914	10	17,684	220
Redeemable preferred stock	31	30	1	
<b>Total fixed maturities</b>	<b>64,705</b>	<b>2,177</b>	<b>62,274</b>	<b>254</b>
<b>Equity securities</b>				
Common stock	467	467		
Non-redeemable preferred stock	128	94	34	
<b>Total equity securities</b>	<b>595</b>	<b>561</b>	<b>34</b>	
<b>Other investments</b>	<b>86</b>	<b>42</b>		<b>44</b>
<b>Total</b>	<b>\$ 65,386</b>	<b>\$ 2,780</b>	<b>\$ 62,308</b>	<b>\$ 298</b>

The Company did not have any transfers between Levels 1 and 2 during the six months ended June 30, 2012.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 4. FAIR VALUE MEASUREMENTS, Continued

(at December 31, 2011, in millions)	Total	Level 1	Level 2	Level 3
<b>Invested assets:</b>				
<b>Fixed maturities</b>				
U.S. Treasury securities and obligations of U.S. government and government agencies and authorities	\$ 2,497	\$ 2,465	\$ 32	\$
Obligations of states, municipalities and political subdivisions	39,022		39,002	20
Debt securities issued by foreign governments	2,318		2,318	
Mortgage-backed securities, collateralized mortgage obligations and pass-through securities	3,515		3,514	1
All other corporate bonds	16,850		16,621	229
Redeemable preferred stock	30	29	1	
<b>Total fixed maturities</b>	<b>64,232</b>	<b>2,494</b>	<b>61,488</b>	<b>250</b>
<b>Equity securities</b>				
Common stock	428	428		
Non-redeemable preferred stock	131	96	35	
<b>Total equity securities</b>	<b>559</b>	<b>524</b>	<b>35</b>	
<b>Other investments</b>	<b>86</b>	<b>42</b>		<b>44</b>
<b>Total</b>	<b>\$ 64,877</b>	<b>\$ 3,060</b>	<b>\$ 61,523</b>	<b>\$ 294</b>

The Company did not have any material transfers between Levels 1 and 2 during the year ended December 31, 2011.

The following tables present the changes in the Level 3 fair value category during the three months and six months ended June 30, 2012 and the twelve months ended December 31, 2011.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****4. FAIR VALUE MEASUREMENTS, Continued**

Three Months Ended June 30, 2012 (in millions)	Fixed Maturities	Other Investments	Total
Balance at March 31, 2012	\$ 250	\$ 44	\$ 294
Total realized and unrealized investment gains (losses):			
Reported in realized investment gains (losses) (1)	1		1
Reported in increases (decreases) in other comprehensive income			
Purchases, sales and settlements/maturities:			
Purchases	33		33
Sales			
Settlements/maturities	(25)		(25)
Gross transfers into Level 3	6		6
Gross transfers out of Level 3	(11)		(11)
Balance at June 30, 2012	\$ 254	\$ 44	\$ 298
Amount of total realized investment gains (losses) for the period included in the consolidated statement of income (loss) attributable to changes in the fair value of assets still held at the reporting date	\$	\$	\$

(1) Includes impairments on investments held at the end of the period.

Six Months Ended June 30, 2012 (in millions)	Fixed Maturities	Other Investments	Total
Balance at December 31, 2011	\$ 250	\$ 44	\$ 294
Total realized and unrealized investment gains (losses):			
Reported in realized investment gains (losses) (1)	2	(1)	1
Reported in increases (decreases) in other comprehensive income	4	1	5
Purchases, sales and settlements/maturities:			
Purchases	50		50
Sales			
Settlements/maturities	(45)		(45)
Gross transfers into Level 3	6		6
Gross transfers out of Level 3	(13)		(13)
Balance at June 30, 2012	\$ 254	\$ 44	\$ 298



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Amount of total realized investment gains (losses) for the period included  
in the consolidated statement of income (loss) attributable to changes in  
the fair value of assets still held at the reporting date

	\$	\$	\$
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(1) Includes impairments on investments held at the end of the period.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****4. FAIR VALUE MEASUREMENTS, Continued**

Twelve Months Ended December 31, 2011 (in millions)	Fixed Maturities	Other Investments	Total
Balance at December 31, 2010	\$ 230	\$ 57	\$ 287
Total realized and unrealized investment gains (losses):			
Reported in realized investment gains (losses) (1)	1	38	39
Reported in increases (decreases) in other comprehensive income		(9)	(9)
Purchases, sales and settlements/maturities:			
Purchases	154	5	159
Sales	(15)	(47)	(62)
Settlements/maturities	(43)		(43)
Gross transfers into Level 3	19		19
Gross transfers out of Level 3 (2)	(96)		(96)
Balance at December 31, 2011	\$ 250	\$ 44	\$ 294
Amount of total realized investment gains (losses) for the period included in the consolidated statement of income attributable to changes in the fair value of assets still held at the reporting date	\$	\$	\$

(1) Includes impairments on investments held at the end of the period.

(2) During the year ended December 31, 2011, approximately \$81 million of municipal fixed maturity securities were valued using observable market data which resulted in a transfer out of Level 3 into Level 2. In prior periods, these securities were valued internally using unobservable inputs.

The Company had no financial assets or financial liabilities that were measured at fair value on a non-recurring basis during the six months ended June 30, 2012 or twelve months ended December 31, 2011.

**Financial Instruments Disclosed, But Not Carried, At Fair Value**

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The Company uses various financial instruments in the normal course of its business. The Company's insurance contracts are excluded from fair value of financial instruments accounting guidance and, therefore, are not included in the amounts discussed below. The following tables present the carrying value and fair value of the Company's financial assets and financial liabilities disclosed, but not carried, at fair value at June 30, 2012 and December 31, 2011, and the level within the fair value hierarchy at which such assets and liabilities are measured on a recurring basis.

(at June 30, 2012, in millions)	Carrying Value	Fair Value	Level 1	Level 2	Level 3
<b>Financial assets:</b>					
Short-term securities	\$ 3,275	\$ 3,275	\$ 1,464	\$ 1,728	\$ 83
<b>Financial liabilities:</b>					
Debt	\$ 6,249	\$ 7,608		\$ 7,266	\$ 342
Commercial paper	100	100		100	

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 4. FAIR VALUE MEASUREMENTS, Continued

(at December 31, 2011, in millions)	Carrying Value	Fair Value	Level 1	Level 2	Level 3
<b>Financial assets:</b>					
Short-term securities	\$ 3,594	\$ 3,594	\$ 2,472	\$ 1,029	\$ 93
<b>Financial liabilities:</b>					
Debt	\$ 6,505	\$ 7,609	\$	\$ 7,057	\$ 552
Commercial paper	100	100		100	

Included in Level 1 short-term securities at June 30, 2012 and December 31, 2011 were amounts held in liquidity investment pools. The Company utilized a pricing service to estimate fair value for approximately 96% and 94% of short-term securities at June 30, 2012 and December 31, 2011, respectively. A description of the process and inputs used by the pricing service to estimate fair value is discussed in the *Fixed Maturities* section above. Estimates of fair value for U.S. Treasury securities and money market funds are based on market quotations received from the pricing service and are disclosed in Level 1 of the hierarchy. The fair value of other short-term fixed maturity securities is estimated by the pricing service using observable market inputs and is disclosed in Level 2 of the hierarchy. For short-term securities where an estimate is not obtained from the pricing service, the carrying value approximates fair value and is included in Level 3 of the hierarchy.

The Company utilized a pricing service to estimate fair value for approximately 96% and 93% of its debt, including commercial paper, at June 30, 2012 and December 31, 2011, respectively. The pricing service utilizes market quotations for debt that have quoted prices in active markets. Since fixed maturities other than U.S. Treasury securities generally do not trade on a daily basis, the fair value estimates are based on market observable inputs and disclosed at Level 2 in the hierarchy. For the small amount of the Company's debt securities for which a pricing service is not used, the Company utilizes pricing estimates from a nationally recognized broker/dealer to estimate fair value. If estimates of fair value are unavailable from the pricing service or the broker/dealer, the Company produces an estimate of fair value based on internally developed valuation techniques which are based on a discounted cash flow methodology and incorporates all available relevant observable market inputs. Estimates of fair value developed internally and from broker quotes are disclosed in Level 3 of the hierarchy.

## 5. GOODWILL AND OTHER INTANGIBLE ASSETS

**Goodwill**

The following table presents the carrying amount of the Company's goodwill by segment at June 30, 2012 and December 31, 2011:

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<b>(in millions)</b>	<b>June 30,</b>	<b>December 31,</b>
	<b>2012</b>	<b>2011</b>
Business Insurance	\$ 2,168	\$ 2,168
Financial, Professional & International Insurance	557	557
Personal Insurance	613	613
Other	27	27
Total	\$ 3,365	\$ 3,365

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 5. GOODWILL AND OTHER INTANGIBLE ASSETS, Continued

## Other Intangible Assets

The following presents a summary of the Company's other intangible assets by major asset class at June 30, 2012 and December 31, 2011:

(at June 30, 2012, in millions)	Gross Carrying Amount		Accumulated Amortization		Net
<b>Intangibles subject to amortization</b>					
Customer-related (1)	\$ 455	\$	\$ 368	\$	\$ 87
Fair value adjustment on claims and claim adjustment expense reserves and reinsurance recoverables (2)	191		89		102
<b>Total intangible assets subject to amortization</b>	<b>646</b>		<b>457</b>		<b>189</b>
<b>Intangible assets not subject to amortization</b>	<b>216</b>				<b>216</b>
<b>Total other intangible assets</b>	<b>\$ 862</b>	<b>\$</b>	<b>\$ 457</b>	<b>\$</b>	<b>\$ 405</b>

(at December 31, 2011, in millions)	Gross Carrying Amount		Accumulated Amortization		Net
<b>Intangibles subject to amortization</b>					
Customer-related	\$ 935	\$	\$ 830	\$	\$ 105
Fair value adjustment on claims and claim adjustment expense reserves and reinsurance recoverables (2)	191		79		112
<b>Total intangible assets subject to amortization</b>	<b>1,126</b>		<b>909</b>		<b>217</b>
<b>Intangible assets not subject to amortization</b>	<b>216</b>				<b>216</b>
<b>Total other intangible assets</b>	<b>\$ 1,342</b>	<b>\$</b>	<b>\$ 909</b>	<b>\$</b>	<b>\$ 433</b>

- 
- (1) Certain intangible assets related to renewal rights became fully amortized during the first quarter of 2012.
- (2) The time value of money and the risk margin (cost of capital) components of the intangible asset run off at different rates, and, as such, the amount recognized in income may be a net benefit in some periods and a net expense in other periods.

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The following presents a summary of the Company's amortization expense for other intangible assets by major asset class:

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Customer-related	\$ 7	\$ 11	\$ 18	\$ 25
Fair value adjustment on claims and claim adjustment expense reserves and reinsurance recoverables	5	6	10	12
<b>Total amortization expense</b>	<b>\$ 12</b>	<b>\$ 17</b>	<b>\$ 28</b>	<b>\$ 37</b>

Intangible asset amortization expense is estimated to be \$24 million for the remainder of 2012, \$45 million in 2013, \$43 million in 2014, \$23 million in 2015 and \$9 million in 2016.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 6. OTHER COMPREHENSIVE INCOME

The following tables present the pretax components of the Company's other comprehensive income, and the related income tax expense (benefit) for each component, for the three months and six months ended June 30, 2012 and 2011.

(for the three months ended June 30, in millions)	Pretax		Tax Expense (Benefit)		Net of Tax	
	2012	2011	2012	2011	2012	2011
<b>Other comprehensive income:</b>						
Change in net unrealized gains on investment securities:						
Having no credit losses recognized in the consolidated statement of income	\$ 216	\$ 645	\$ 77	\$ 224	\$ 139	\$ 421
Having credit losses recognized in the consolidated statement of income	5	(10)	1	(4)	4	(6)
Net changes in benefit plan assets and obligations	22	19	8	7	14	12
Net changes in unrealized foreign currency translation and other changes	(86)	16	(20)	4	(66)	12
<b>Other comprehensive income</b>	<b>\$ 157</b>	<b>\$ 670</b>	<b>\$ 66</b>	<b>\$ 231</b>	<b>\$ 91</b>	<b>\$ 439</b>

(for the six months ended June 30, in millions)	Pretax		Tax Expense (Benefit)		Net of Tax	
	2012	2011	2012	2011	2012	2011
<b>Other comprehensive income:</b>						
Change in net unrealized gains on investment securities:						
Having no credit losses recognized in the consolidated statement of income	\$ 139	\$ 539	\$ 50	\$ 189	\$ 89	\$ 350
Having credit losses recognized in the consolidated statement of income	30	18	10	6	20	12
Net changes in benefit plan assets and obligations	42	37	15	13	27	24
Net changes in unrealized foreign currency translation and other changes	(22)	86	(11)	16	(11)	70
<b>Other comprehensive income</b>	<b>\$ 189</b>	<b>\$ 680</b>	<b>\$ 64</b>	<b>\$ 224</b>	<b>\$ 125</b>	<b>\$ 456</b>





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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**7. SHAREHOLDERS EQUITY**

*Share Repurchase Authorization.* The Company's board of directors has approved common share repurchase authorizations under which repurchases may be made from time to time in the open market, pursuant to pre-set trading plans meeting the requirements of Rule 10b5-1 under the Securities Exchange Act of 1934, in private transactions or otherwise. The authorizations do not have a stated expiration date. The timing and actual number of shares to be repurchased in the future will depend on a variety of factors, including the Company's financial position, earnings, common share price, catastrophe losses, funding of the Company's qualified pension plan, capital requirements of the Company's operating subsidiaries, legal requirements, regulatory constraints, other investment opportunities (including mergers and acquisitions), market conditions and other factors. During the three months and six months ended June 30, 2012, the Company repurchased 5.6 million and 11.6 million shares, respectively, under its share repurchase authorization, for a total cost of approximately \$350 million and \$700 million, respectively. The average cost per share repurchased was \$62.40 and \$60.51, respectively. At June 30, 2012, the Company had \$2.91 billion of capacity remaining under the share repurchase authorization.

*Conversion of Preferred Stock to Common Stock.* In May 2011, the Company's board of directors authorized the redemption of the Company's preferred stock held by The Travelers 401(k) Savings Plan (the Savings Plan) and gave notice of that redemption to the appropriate fiduciaries of the Savings Plan. Following a fiduciary review, the Savings Plan exercised its right to convert each preferred share into eight shares of the Company's common stock. As a result, all preferred shares outstanding on June 7, 2011 (190,083 shares) were converted into a total of 1.52 million shares of the Company's common stock.

**8. DEBT**

On May 29, 2012, the Company purchased and retired \$8.5 million aggregate principal amount of its 6.25% fixed-to-floating rate junior subordinated debentures due March 15, 2067. On June 15, 2012, the Company's \$250 million, 5.375% senior notes matured and were fully paid.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 9. EARNINGS PER SHARE

The following is a reconciliation of the net income (loss) and share data used in the basic and diluted earnings per share computations for the periods presented:

(in millions, except per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Basic</b>				
Net income (loss), as reported	\$ 499	\$ (364)	\$ 1,305	\$ 475
Participating share-based awards allocated income	(4)	(2)	(10)	(4)
Preferred stock dividends				(1)
Net income (loss) available to common shareholders basic	\$ 495	\$ (366)	\$ 1,295	\$ 470
<b>Diluted</b>				
Net income (loss) available to common shareholders	\$ 495	\$ (366)	\$ 1,295	\$ 470
Effect of dilutive securities:				
Convertible preferred stock				1
Net income (loss) available to common shareholders diluted	\$ 495	\$ (366)	\$ 1,295	\$ 471
<b>Common Shares</b>				
<b>Basic</b>				
Weighted average shares outstanding	388.0	418.6	390.0	423.3
<b>Diluted</b>				
Weighted average shares outstanding	388.0	418.6	390.0	423.3
Weighted average effects of dilutive securities:				
Stock options and performance shares	3.6		3.5	4.4
Convertible preferred stock				1.4
Total	391.6	418.6	393.5	429.1
<b>Net Income (Loss) per Common Share</b>				
Basic	\$ 1.27	\$ (0.88)	\$ 3.32	\$ 1.11
Diluted	\$ 1.26	\$ (0.88)	\$ 3.29	\$ 1.10

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Net loss per basic and diluted common share for the three months ended June 30, 2011 excluded the allocation of \$4.6 million of undistributed loss to participating share-based awards, since such allocation would result in anti-dilution of basic and diluted earnings per share for the three months ended June 30, 2011. In addition, the net loss per diluted common share for the three months ended June 30, 2011 excluded the weighted average effects of 4.6 million stock options and performance shares, and convertible preferred stock convertible into 1.2 million common shares. The impact of these potential shares of common stock and their effects on income were excluded from the calculation of net loss per share on a diluted basis as their effect was anti-dilutive for the three months ended June 30, 2011.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****10. SHARE-BASED INCENTIVE COMPENSATION**

The following information relates to fully vested stock option awards at June 30, 2012:

<b>Stock Options</b>	<b>Number</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Contractual Life Remaining</b>	<b>Aggregate Intrinsic Value (\$ in millions)</b>
Vested at end of period (1)	<b>11,030,213</b>	<b>\$ 47.95</b>	<b>5.2 years</b>	<b>\$ 175</b>
Exercisable at end of period	<b>8,017,683</b>	<b>\$ 45.05</b>	<b>3.9 years</b>	<b>\$ 151</b>

(1) Represents awards for which the requisite service has been rendered, including those that are retirement eligible.

The total compensation cost for all share-based incentive compensation awards recognized in earnings was \$28 million and \$30 million for the three months ended June 30, 2012 and 2011, respectively, and \$66 million and \$67 million for the six months ended June 30, 2012 and 2011, respectively. The related tax benefits recognized in the consolidated statement of income (loss) was \$10 million for each of the three months ended June 30, 2012 and 2011, and \$23 million for each of the six months ended June 30, 2012 and 2011.

The total unrecognized compensation cost related to all nonvested share-based incentive compensation awards at June 30, 2012 was \$161 million, which is expected to be recognized over a weighted-average period of 2.0 years. The total unrecognized compensation cost related to all nonvested share-based incentive compensation awards at December 31, 2011 was \$114 million, which was expected to be recognized over a weighted-average period of 1.7 years.

**11. PENSION PLANS, RETIREMENT BENEFITS AND SAVINGS PLANS**

The following tables summarize the components of net periodic benefit cost for the Company's pension and postretirement benefit plans recognized in the consolidated statement of income (loss).

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(for the three months ended June 30, in millions)	Pension Plans		Postretirement Benefit Plans	
	2012	2011	2012	2011
<b>Net Periodic Benefit Cost:</b>				
Service cost	\$ 29	\$ 24	\$	\$
Interest cost on benefit obligation	34	34	3	4
Expected return on plan assets	(47)	(45)	(1)	(1)
Amortization of unrecognized:				
Prior service benefit				
Net actuarial loss	23	19		
Net benefit expense	\$ 39	\$ 32	\$ 2	\$ 3

(for the six months ended June 30, in millions)	Pension Plans		Postretirement Benefit Plans	
	2012	2011	2012	2011
<b>Net Periodic Benefit Cost:</b>				
Service cost	\$ 57	\$ 49	\$	\$
Interest cost on benefit obligation	69	68	6	7
Expected return on plan assets	(94)	(91)	(1)	(1)
Amortization of unrecognized:				
Prior service benefit				
Net actuarial loss	45	38		
Net benefit expense	\$ 77	\$ 64	\$ 5	\$ 6

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**12. CONTINGENCIES, COMMITMENTS AND GUARANTEES**

**Contingencies**

The major pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the Company or any of its subsidiaries is a party or to which any of the Company's properties is subject are described below.

***Asbestos- and Environmental-Related Proceedings***

In the ordinary course of its insurance business, the Company receives claims for insurance arising under policies issued by the Company asserting alleged injuries and damages from asbestos- and environmental-related exposures that are the subject of related coverage litigation, including, among others, the litigation described below. The Company is defending asbestos- and environmental-related litigation vigorously and believes that it has meritorious defenses; however, the outcomes of these disputes are uncertain. In this regard, the Company employs dedicated specialists and aggressive resolution strategies to manage asbestos and environmental loss exposure, including settling litigation under appropriate circumstances.

***Asbestos Direct Action Litigation*** In October 2001 and April 2002, two purported class action suits (*Wise v. Travelers* and *Meninger v. Travelers*) were filed against Travelers Property Casualty Corp. (TPC) and other insurers (not including The St. Paul Companies, Inc. (SPC)) in state court in West Virginia. These and other cases subsequently filed in West Virginia were consolidated into a single proceeding in the Circuit Court of Kanawha County, West Virginia. The plaintiffs allege that the insurer defendants engaged in unfair trade practices in violation of state statutes by inappropriately handling and settling asbestos claims. The plaintiffs seek to reopen large numbers of settled asbestos claims and to impose liability for damages, including punitive damages, directly on insurers. Similar lawsuits alleging inappropriate handling and settling of asbestos claims were filed in Massachusetts and Hawaii state courts. These suits are collectively referred to as the Statutory and Hawaii Actions.

In March 2002, the plaintiffs in consolidated asbestos actions pending before a mass tort panel of judges in West Virginia state court amended their complaint to include TPC as a defendant, alleging that TPC and other insurers breached alleged duties to certain users of asbestos products. The plaintiffs seek damages, including punitive damages. Lawsuits seeking similar relief and raising similar allegations, primarily violations of purported common law duties to third parties, have also been asserted in various state courts against TPC and SPC. The claims asserted in these suits are collectively referred to as the Common Law Claims.

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The federal bankruptcy court that had presided over the bankruptcy of TPC's former policyholder Johns-Manville Corporation issued a temporary injunction prohibiting the prosecution of the Statutory Actions (but not the Hawaii Actions), the Common Law Claims and an additional set of cases filed in various state courts in Texas and Ohio, and enjoining certain attorneys from filing any further lawsuits against TPC based on similar allegations. Notwithstanding the injunction, additional common law claims were filed against TPC.

In November 2003, the parties reached a settlement of the Statutory and Hawaii Actions. This settlement includes a lump-sum payment of up to \$412 million by TPC, subject to a number of significant contingencies. In May 2004, the parties reached a settlement resolving substantially all pending and similar future Common Law Claims against TPC. This settlement requires a payment of up to \$90 million by TPC, subject to a number of significant contingencies. Among the contingencies for each of these settlements is a final order of the bankruptcy court clarifying that all of these claims, and similar future asbestos-related claims against TPC, are barred by prior orders entered by the bankruptcy court ( the 1986 Orders ).

On August 17, 2004, the bankruptcy court entered an order approving the settlements and clarifying that the 1986 Orders barred the pending Statutory and Hawaii Actions and substantially all Common Law Claims pending against TPC ( the Clarifying Order ). The Clarifying Order also applies to similar direct action claims that may be filed in the future.

On March 29, 2006, the U.S. District Court for the Southern District of New York substantially affirmed the Clarifying Order while vacating that portion of the order that required all future direct actions against TPC to first be approved by the bankruptcy court before proceeding in state or federal court.



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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**12. CONTINGENCIES, COMMITMENTS AND GUARANTEES, Continued**

Various parties appealed the district court's March 29, 2006 ruling to the U.S. Court of Appeals for the Second Circuit. On February 15, 2008, the Second Circuit issued an opinion vacating on jurisdictional grounds the District Court's approval of the Clarifying Order. On February 29, 2008, TPC and certain other parties to the appeals filed petitions for rehearing and/or rehearing *en banc*, requesting reinstatement of the district court's judgment, which were denied. TPC and certain other parties filed Petitions for Writ of Certiorari in the United States Supreme Court seeking review of the Second Circuit's decision, and on December 12, 2008, the Petitions were granted.

On June 18, 2009, the Supreme Court ruled in favor of TPC, reversing the Second Circuit's February 15, 2008 decision, finding, among other things, that the 1986 Orders are final and generally bar the Statutory and Hawaii actions and substantially all Common Law Claims against TPC. Further, the Supreme Court ruled that the bankruptcy court had jurisdiction to issue the Clarifying Order. However, since the Second Circuit had not ruled on certain additional issues, principally related to procedural matters and the adequacy of notice provided to certain parties, the Supreme Court remanded the case to the Second Circuit for further proceedings on those specific issues. On October 21, 2009, all but one of the objectors to the Clarifying Order requested that the Second Circuit dismiss their appeal of the order approving the settlement, and that request was granted.

On March 22, 2010, the Second Circuit issued an opinion in which it found that the notice of the 1986 Orders provided to the remaining objector was insufficient to bar contribution claims by that objector against TPC. On April 5, 2010, TPC filed a Petition for Rehearing and Rehearing *En Banc* with the Second Circuit, requesting further review of its March 22, 2010 opinion, which was denied on May 25, 2010. On August 18, 2010, TPC filed a Petition for Writ of Certiorari in the United States Supreme Court seeking review of the Second Circuit's March 22, 2010 opinion, and a Petition for a Writ of Mandamus seeking an order from the Supreme Court requiring the Second Circuit to comply with the Supreme Court's June 18, 2009 ruling in TPC's favor. The Supreme Court denied the Petitions on November 29, 2010.

The plaintiffs in the Statutory and Hawaii actions and the Common Law Claims actions filed Motions to Compel with the bankruptcy court on September 2, 2010 and September 3, 2010, respectively, arguing that all conditions precedent to the settlements have been met and seeking to require TPC to pay the settlement amounts. On September 30, 2010, TPC filed an Opposition to the plaintiffs' Motions to Compel on the grounds that the conditions precedent to the settlements, principally the requirement that all contribution claims be barred, have not been met in light of the Second Circuit's March 22, 2010 opinion. On December 16, 2010, the bankruptcy court granted the plaintiffs' motions and ruled that TPC was required to fund the settlements. On January 20, 2011, the bankruptcy court entered judgment in accordance with its December 16, 2010 ruling and ordered TPC to pay the settlement amounts plus prejudgment interest. On January 21, 2011, TPC filed an appeal with the U.S. District Court for the Southern District of New York from the bankruptcy court's January 20, 2011 judgment. On January 24, 2011, certain of the plaintiffs in the Common Law Claims actions appealed that portion of the bankruptcy court's January 20, 2011 judgment that denied their request for an order of contempt and for sanctions. On March 1, 2012, the district court ruled in TPC's favor and reversed the bankruptcy court, finding that the conditions to the settlements had not been met, and that TPC is not obligated to pay the settlement amounts. The district court also upheld the bankruptcy court's order denying the plaintiffs' motion for an order of contempt and for sanctions. The district court further ruled that, since TPC is not obligated to go forward with the settlements, it was unnecessary to address the issue of pre-judgment interest. The plaintiffs appealed the district court's March 1, 2012 decision to the Second Circuit Court of Appeals, and those appeals are pending.

SPC, which is not covered by the Manville bankruptcy court rulings or the settlements described above, is a party to pending direct action cases in Texas state court asserting common law claims. All such cases that are still pending and in which SPC has been served are currently on the inactive docket in Texas state court. If any of those cases becomes active, SPC intends to litigate those cases vigorously. SPC was previously a defendant in similar direct actions in Ohio state court. Those actions have all been dismissed following favorable rulings by Ohio trial and appellate courts. From time to time, SPC and/or its subsidiaries have been named in individual direct actions in other jurisdictions.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**12. CONTINGENCIES, COMMITMENTS AND GUARANTEES, Continued**

*Outcome and Impact of Asbestos and Environmental Claims and Litigation.* Currently, it is not possible to predict legal outcomes and their impact on the future development of claims and litigation relating to asbestos and environmental claims. Any such development will be affected by future court decisions and interpretations, as well as changes in applicable legislation. Because of these uncertainties, additional liabilities may arise for amounts in excess of the Company's current reserves. In addition, the Company's estimate of ultimate claims and claim adjustment expenses may change. These additional liabilities or increases in estimates, or a range of either, cannot now be reasonably estimated and could result in income statement charges that could be material to the Company's results of operations in future periods.

*Other Proceedings Not Arising Under Insurance Contracts or Reinsurance Agreements*

*Broker Anti-Trust Litigation* In 2005, four putative class action lawsuits were brought against a number of insurance brokers and insurers, including the Company, by plaintiffs who allegedly purchased insurance products through one or more of the defendant brokers. The plaintiffs alleged that various insurance brokers conspired with each other and with various insurers, including the Company, to artificially inflate premiums, allocate brokerage customers and rig bids for insurance products offered to those customers. To the extent they were not originally filed there, the federal class actions were transferred to the U.S. District Court for the District of New Jersey and were consolidated for pre-trial proceedings with other class actions under the caption *In re Insurance Brokerage Antitrust Litigation*. On August 1, 2005, various plaintiffs, including the four named plaintiffs in the above-referenced class actions, filed an amended consolidated class action complaint naming various brokers and insurers, including the Company, on behalf of a putative nationwide class of policyholders. The complaint included causes of action under the Sherman Act, the Racketeer Influenced and Corrupt Organizations Act (RICO), state common law and the laws of the various states prohibiting antitrust violations. The complaint sought monetary damages, including punitive damages and trebled damages, permanent injunctive relief, restitution, including disgorgement of profits, interest and costs, including attorneys' fees. All defendants moved to dismiss the complaint for failure to state a claim. After giving plaintiffs multiple opportunities to replead, the court dismissed the Sherman Act claims on August 31, 2007 and the RICO claims on September 28, 2007, both with prejudice, and declined to exercise supplemental jurisdiction over the state law claims. The plaintiffs appealed the district court's decisions to the U.S. Court of Appeals for the Third Circuit. On August 16, 2010, the Third Circuit affirmed the district court's dismissal of all Sherman Act and RICO claims against certain defendants, including the Company, except for Sherman Act and RICO claims involving the sale of excess casualty insurance through a single defendant broker, as well as all state law claims, which they remanded to the district court for further proceedings. On October 1, 2010, defendants, including the Company, filed renewed motions to dismiss the remanded claims. On March 18, 2011, the Company and certain other defendants entered into an agreement with the plaintiffs to settle the lawsuit, under which the Company agreed to pay \$6.75 million. Preliminary approval of the settlement was granted on June 27, 2011. On September 14, 2011, the court conducted a final fairness hearing, and on March 30, 2012, the court granted final approval of the settlement. On April 27, 2012, three members of the settlement class appealed the court's order granting final approval of the settlement to the U.S. Court of Appeals for the Third Circuit. Those appeals are pending.

*Other* In addition to those described above, the Company is involved in other lawsuits, including lawsuits alleging extra-contractual damages relating to insurance contracts or reinsurance agreements, that do not arise under insurance contracts or reinsurance agreements. Based upon currently available information, the Company does not believe it is reasonably possible that any such lawsuit or related lawsuits would be

material to the Company's results of operations or have a material adverse effect on the Company's financial position or liquidity.

***Gain Contingencies***

On August 20, 2010, in a reinsurance dispute in New York state court captioned *United States Fidelity & Guaranty Company v. American Re-Insurance Company, et al.*, the trial court granted summary judgment for United States Fidelity and Guaranty Company (USF&G), a subsidiary of the Company, and on October 25, 2010, entered judgment against American Re-Insurance Company, a subsidiary of Munich Re (American Re) and three other reinsurers, awarding USF&G \$251 million plus pre-judgment interest in the amount of \$169 million. The judgment, including the award of interest, was appealed by the reinsurers to the New York Supreme Court, Appellate Division, First Department. On January 24, 2012, the Appellate Division affirmed the judgment, which, as of that date, totaled \$467 million, comprising the judgment of \$251 million and interest of \$216 million (including post-judgment interest). Post-judgment interest continues to accrue (without

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**12. CONTINGENCIES, COMMITMENTS AND GUARANTEES, Continued**

compounding) at the rate of 9% until the judgment is paid. At June 30, 2012, the judgment, including post-judgment interest, totaled \$484 million. On January 30, 2012, the reinsurers filed a motion with the Appellate Division seeking permission to appeal its decision to the New York Court of Appeals, and on March 12, 2012, the Appellate Division granted the reinsurers' motion. The reinsurers' appeal is pending. The \$251 million awarded by the court represents the amount owed to USF&G under the terms of the disputed reinsurance agreements and is reported as part of reinsurance recoverables in the Company's consolidated balance sheet. The interest awarded by the Court, including post-judgment interest, is treated for accounting purposes as a gain contingency in accordance with FASB Topic 450, *Contingencies*, and accordingly has not been recognized in the Company's consolidated financial statements.

In an unrelated action, The Travelers Indemnity Company is one of the Settlement Class plaintiffs and a class member in a class action lawsuit captioned *Safeco Insurance Company of America, et al. v. American International Group, Inc. et al.* (U.S. District Court, N.D. Ill.) in which the defendants are alleged to have engaged in the under-reporting of workers' compensation premium in connection with a workers' compensation reinsurance pool in which several subsidiaries of the Company participate. On July 26, 2011, the court granted preliminary approval of a class settlement pursuant to which the defendants agreed to pay \$450 million to the class. The settlement includes a plan of allocation of the settlement proceeds among the class members. On December 21, 2011, the court entered an order granting final approval of the settlement, and on February 28, 2012, the district court issued a written opinion regarding its approval of the settlement. Three parties who objected to the settlement have appealed the court's orders approving the settlement to the U.S. Court of Appeals for the Seventh Circuit. The Company anticipates that its allocation from the settlement fund, in the event the court's approval of the class settlement is affirmed, will be approximately \$90 million. This amount is treated for accounting purposes as a gain contingency in accordance with FASB Topic 450, *Contingencies*, and accordingly has not been recognized in the Company's consolidated financial statements.

**Other Commitments and Guarantees**

**Commitments**

*Investment Commitments* The Company has unfunded commitments to private equity limited partnerships and real estate partnerships in which it invests. These commitments totaled \$1.18 billion and \$1.15 billion at June 30, 2012 and December 31, 2011, respectively.

**Guarantees**

In the ordinary course of selling business entities to third parties, the Company has agreed to indemnify purchasers for losses arising out of breaches of representations and warranties with respect to the business entities being sold, covenants and obligations of the Company and/or its subsidiaries following the closing, and in certain cases obligations arising from undisclosed liabilities, adverse reserve development, imposition of additional taxes due to either a change in the tax law or an adverse interpretation of the tax law, or certain named litigation. Such indemnification provisions generally survive for periods ranging from seven years following the applicable closing date to the expiration of the relevant statutes of limitations, although, in some cases, there may be other agreed upon term limitations or no term limitations. Certain of these contingent obligations are subject to deductibles which have to be incurred by the obligee before the Company is obligated to make payments. The maximum amount of the Company's contingent obligation for indemnifications related to the sale of business entities that are quantifiable was \$1.22 billion at June 30, 2012, of which \$9 million was recognized on the balance sheet at that date.

The Company also has contingent obligations for guarantees related to certain investments, third-party loans related to certain investments, certain insurance policy obligations of former insurance subsidiaries, and various other indemnifications. The Company also provides standard indemnifications to service providers in the normal course of business. The indemnification clauses are often standard contractual terms. Certain of these guarantees and indemnifications have no stated or notional amounts or limitation to the maximum potential future payments, and, accordingly, the Company is unable to develop an estimate of the maximum potential payments for such arrangements. The maximum amount of the Company's obligation for guarantees of certain investments and third-party loans related to certain investments that are quantifiable was \$126 million at June 30, 2012, approximately \$63 million of which is indemnified by a third party. The maximum amount of the Company's obligation related to the guarantee of certain insurance policy obligations of a former insurance subsidiary was \$480 million at June 30, 2012, all of which is indemnified by a third party.

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**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued**

**13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES**

The following consolidating financial statements of the Company have been prepared pursuant to Rule 3-10 of Regulation S-X. These consolidating financial statements have been prepared from the Company's financial information on the same basis of accounting as the consolidated financial statements. The Travelers Companies, Inc. has fully and unconditionally guaranteed certain debt obligations of TPC, its wholly-owned subsidiary, which totaled \$1.20 billion at June 30, 2012.

Prior to the merger of TPC and SPC in 2004, TPC fully and unconditionally guaranteed the payment of all principal, premiums, if any, and interest on certain debt obligations of its wholly-owned subsidiary, Travelers Insurance Group Holdings, Inc. (TIGHI). The Travelers Companies, Inc. has fully and unconditionally guaranteed such guarantee obligations of TPC. TPC is deemed to have no assets or operations independent of TIGHI. Consolidating financial information for TIGHI has not been presented herein because such financial information would be substantially the same as the financial information provided for TPC.

Table of Contents**THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued****13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES, Continued****CONSOLIDATING STATEMENT OF INCOME (Unaudited)**

For the three months ended June 30, 2012

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Revenues</b>					
Premiums	\$ 3,745	\$ 1,784	\$ 2	\$	\$ 5,529
Net investment income	507	229	2		738
Fee income	58	1			59
Net realized investment gains	3	1			4
Other revenues	22	7			29
<b>Total revenues</b>	<b>4,335</b>	<b>2,022</b>	<b>2</b>		<b>6,359</b>
<b>Claims and expenses</b>					
Claims and claim adjustment expenses	2,549	1,237			3,786
Amortization of deferred acquisition costs	647	329			976
General and administrative expenses	608	284	1		893
Interest expense	18		78		96
<b>Total claims and expenses</b>	<b>3,822</b>	<b>1,850</b>	<b>79</b>		<b>5,751</b>
<b>Income (loss) before income taxes</b>	<b>513</b>	<b>172</b>	<b>(77)</b>		<b>608</b>
Income tax expense (benefit)	119	27	(37)		109
Equity in net income of subsidiaries			539	(539)	
<b>Net income</b>	<b>\$ 394</b>	<b>\$ 145</b>	<b>\$ 499</b>	<b>\$ (539)</b>	<b>\$ 499</b>

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net Realized Investment Gains</b>					
Other-than-temporary impairment losses:					
Total gains (losses)	\$ (1)	\$ 12	\$	\$	\$ 11
Non-credit component of impairments recognized in accumulated other comprehensive income	(2)	(13)			(15)



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Other-than-temporary impairment losses	(3)	(1)	(4)
Other net realized investment gains	6	2	8
<b>Net realized investment gains</b>	<b>\$ 3</b>	<b>\$ 1</b>	<b>\$ 4</b>

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(1) The Travelers Companies, Inc., excluding its subsidiaries.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES, Continued

## CONSOLIDATING STATEMENT OF INCOME (LOSS) (Unaudited)

For the three months ended June 30, 2011

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Revenues</b>					
Premiums	\$ 3,710	\$ 1,793	\$ 2	\$	\$ 5,503
Net investment income	511	245	2		758
Fee income	73	1			74
Net realized investment gains (losses)	12	11	(4)		19
Other revenues	27	7			34
<b>Total revenues</b>	<b>4,333</b>	<b>2,057</b>	<b>(2)</b>		<b>6,388</b>
<b>Claims and expenses</b>					
Claims and claim adjustment expenses	3,431	1,710			5,141
Amortization of deferred acquisition costs	641	329			970
General and administrative expenses	591	290	26		907
Interest expense	18		79		97
<b>Total claims and expenses</b>	<b>4,681</b>	<b>2,329</b>	<b>105</b>		<b>7,115</b>
<b>Loss before income taxes</b>	<b>(348)</b>	<b>(272)</b>	<b>(107)</b>		<b>(727)</b>
Income tax benefit	(204)	(126)	(33)		(363)
Equity in net loss of subsidiaries			(290)	290	
<b>Net loss</b>	<b>\$ (144)</b>	<b>\$ (146)</b>	<b>\$ (364)</b>	<b>\$ 290</b>	<b>\$ (364)</b>

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net Realized Investment Gains (Losses)</b>					
Other-than-temporary impairment losses:					
Total gains (losses)	\$ (3)	\$ 8	\$	\$	\$ 5
Non-credit component of impairments recognized in accumulated other comprehensive income		(9)			(9)

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Other-than-temporary impairment losses	(3)	(1)	(4)	
Other net realized investment gains (losses)	15	12	(4)	23
<b>Net realized investment gains (losses)</b>	<b>\$ 12</b>	<b>\$ 11</b>	<b>\$ (4)</b>	<b>\$ 19</b>

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(1) The Travelers Companies, Inc., excluding its subsidiaries.

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For the six months ended June 30, 2012

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Revenues</b>					
Premiums	\$ 7,488	\$ 3,564	\$	\$	\$ 11,052
Net investment income	1,001	473	4		1,478
Fee income	140	1			141
Net realized investment gains (losses)	15	(1)			14
Other revenues	49	17			66
<b>Total revenues</b>	<b>8,693</b>	<b>4,054</b>	<b>4</b>		<b>12,751</b>
<b>Claims and expenses</b>					
Claims and claim adjustment expenses	4,821	2,329			7,150
Amortization of deferred acquisition costs	1,293	654			1,947
General and administrative expenses	1,207	566	4		1,777
Interest expense	36		156		192
<b>Total claims and expenses</b>	<b>7,357</b>	<b>3,549</b>	<b>160</b>		<b>11,066</b>
<b>Income (loss) before income taxes</b>	<b>1,336</b>	<b>505</b>	<b>(156)</b>		<b>1,685</b>
Income tax expense (benefit)	324	111	(55)		380
Equity in net income of subsidiaries			1,406	(1,406)	
<b>Net income</b>	<b>\$ 1,012</b>	<b>\$ 394</b>	<b>\$ 1,305</b>	<b>\$ (1,406)</b>	<b>\$ 1,305</b>

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net Realized Investment Gains (Losses)</b>					
Other-than-temporary impairment losses:					
Total gains	\$	\$ 11	\$	\$	\$ 11
Non-credit component of impairments recognized in accumulated other comprehensive income	(6)	(13)			(19)

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Other-than-temporary impairment losses	(6)	(2)	(8)
Other net realized investment gains (losses)	21	1	22
<b>Net realized investment gains (losses)</b>	<b>\$ 15</b>	<b>\$ (1)</b>	<b>\$ 14</b>

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(1) The Travelers Companies, Inc., excluding its subsidiaries.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES, Continued

## CONSOLIDATING STATEMENT OF INCOME (Unaudited)

For the six months ended June 30, 2011

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Revenues</b>					
Premiums	\$ 7,335	\$ 3,539	\$	\$	\$ 10,874
Net investment income	1,043	489	5		1,537
Fee income	147	1			148
Net realized investment gains (losses)	21	23	(5)		39
Other revenues	57	11			68
<b>Total revenues</b>	<b>8,603</b>	<b>4,063</b>			<b>12,666</b>
<b>Claims and expenses</b>					
Claims and claim adjustment expenses	5,665	2,858			8,523
Amortization of deferred acquisition costs	1,267	651			1,918
General and administrative expenses	1,187	580	23		1,790
Interest expense	36		157		193
<b>Total claims and expenses</b>	<b>8,155</b>	<b>4,089</b>	<b>180</b>		<b>12,424</b>
<b>Income (loss) before income taxes</b>	<b>448</b>	<b>(26)</b>	<b>(180)</b>		<b>242</b>
Income tax benefit	(8)	(69)	(156)		(233)
Equity in net income of subsidiaries			499	(499)	
<b>Net income</b>	<b>\$ 456</b>	<b>\$ 43</b>	<b>\$ 475</b>	<b>\$ (499)</b>	<b>\$ 475</b>

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net Realized Investment Gains (Losses)</b>					
Other-than-temporary impairment losses:					
Total gains (losses)	\$ (1)	\$ 8	\$	\$	\$ 7
Non-credit component of impairments recognized in accumulated other comprehensive income	(5)	(10)			(15)

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Other-than-temporary impairment losses	(6)	(2)	(8)
Other net realized investment gains (losses)	27	25	(5)
<b>Net realized investment gains (losses)</b>	<b>\$ 21</b>	<b>\$ 23</b>	<b>\$ (5)</b>

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(1) The Travelers Companies, Inc., excluding its subsidiaries.

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For the three months ended June 30, 2012

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net income</b>	\$ 394	\$ 145	\$ 499	\$ (539)	\$ 499
<b>Other comprehensive income:</b>					
Change in net unrealized gains on investment securities:					
Having no credit losses recognized in the consolidated statement of income	167	52	216	(219)	216
Having credit losses recognized in the consolidated statement of income	5		5	(5)	5
Net changes in benefit plan assets and obligations		1	22	(1)	22
Net changes in unrealized foreign currency translation and other changes	(54)	(32)	(86)	86	(86)
<b>Other comprehensive income before income taxes</b>	118	21	157	(139)	157
Income tax expense	43	16	66	(59)	66
<b>Other comprehensive income, net of taxes</b>	75	5	91	(80)	91
<b>Comprehensive income</b>	\$ 469	\$ 150	\$ 590	\$ (619)	\$ 590

(1) The Travelers Companies, Inc., excluding its subsidiaries.



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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES,  
Continued

## CONSOLIDATING STATEMENT OF COMPREHENSIVE INCOME (Unaudited)

For the three months ended June 30, 2011

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net loss</b>	\$ (144)	\$ (146)	\$ (364)	\$ 290	\$ (364)
<b>Other comprehensive income:</b>					
Change in net unrealized gains on investment securities:					
Having no credit losses recognized in the consolidated statement of income (loss)	441	204	645	(645)	645
Having credit losses recognized in the consolidated statement of income (loss)	(8)	(2)	(10)	10	(10)
Net changes in benefit plan assets and obligations			19		19
Net changes in unrealized foreign currency translation and other changes	13	4	16	(17)	16
<b>Other comprehensive income before income taxes</b>	446	206	670	(652)	670
Income tax expense	154	71	231	(225)	231
<b>Other comprehensive income, net of taxes</b>	292	135	439	(427)	439
<b>Comprehensive income (loss)</b>	\$ 148	\$ (11)	\$ 75	\$ (137)	\$ 75

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(1) The Travelers Companies, Inc., excluding its subsidiaries.

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For the six months ended June 30, 2012

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net income</b>	\$ 1,012	\$ 394	\$ 1,305	\$ (1,406)	\$ 1,305
<b>Other comprehensive income:</b>					
Change in net unrealized gains on investment securities:					
Having no credit losses recognized in the consolidated statement of income	113	20	139	(133)	139
Having credit losses recognized in the consolidated statement of income	21	9	30	(30)	30
Net changes in benefit plan assets and obligations			42		42
Net changes in unrealized foreign currency translation and other changes	(33)	11	(22)	22	(22)
<b>Other comprehensive income before income taxes</b>	101	40	189	(141)	189
Income tax expense	36	11	64	(47)	64
<b>Other comprehensive income, net of taxes</b>	65	29	125	(94)	125
<b>Comprehensive income</b>	\$ 1,077	\$ 423	\$ 1,430	\$ (1,500)	\$ 1,430

(1) The Travelers Companies, Inc., excluding its subsidiaries.

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For the six months ended June 30, 2011

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Net income</b>	\$ 456	\$ 43	\$ 475	\$ (499)	\$ 475
<b>Other comprehensive income:</b>					
Change in net unrealized gains on investment securities:					
Having no credit losses recognized in the consolidated statement of income (loss)	371	165	539	(536)	539
Having credit losses recognized in the consolidated statement of income (loss)	2	16	18	(18)	18
Net changes in benefit plan assets and obligations			37		37
Net changes in unrealized foreign currency translation and other changes	35	51	86	(86)	86
<b>Other comprehensive income before income taxes</b>	408	232	680	(640)	680
Income tax expense	140	70	224	(210)	224
<b>Other comprehensive income, net of taxes</b>	268	162	456	(430)	456
<b>Comprehensive income</b>	\$ 724	\$ 205	\$ 931	\$ (929)	\$ 931

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(1) The Travelers Companies, Inc., excluding its subsidiaries.

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At June 30, 2012

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Assets</b>					
Fixed maturities, available for sale, at fair value (amortized cost \$60,313)	\$ 44,014	\$ 20,657	\$ 34	\$	\$ 64,705
Equity securities, available for sale, at fair value (cost \$436)	147	348	100		595
Real estate investments	33	866			899
Short-term securities	1,095	269	1,911		3,275
Other investments	2,395	1,074	1		3,470
<b>Total investments</b>	<b>47,684</b>	<b>23,214</b>	<b>2,046</b>		<b>72,944</b>
Cash	110	116	4		230
Investment income accrued	509	242			751
Premiums receivable	4,130	2,067			6,197
Reinsurance recoverables	6,825	3,579			10,404
Ceded unearned premiums	670	204			874
Deferred acquisition costs	1,586	253			1,839
Contractholder receivables	3,563	1,340			4,903
Goodwill	2,411	954			3,365
Other intangible assets	283	122			405
Investment in subsidiaries			28,353	(28,353)	
Other assets	2,064	22	332		2,418
<b>Total assets</b>	<b>\$ 69,835</b>	<b>\$ 32,113</b>	<b>\$ 30,735</b>	<b>\$ (28,353)</b>	<b>\$ 104,330</b>
<b>Liabilities</b>					
Claims and claim adjustment expense reserves	\$ 33,415	\$ 17,378	\$	\$	\$ 50,793
Unearned premium reserves	7,835	3,614			11,449
Contractholder payables	3,563	1,340			4,903
Payables for reinsurance premiums	198	215			413
Deferred taxes	229	93	(128)		194
Debt	1,191		5,158		6,349

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Other liabilities	3,869	645	666	5,180
<b>Total liabilities</b>	<b>50,300</b>	<b>23,285</b>	<b>5,696</b>	<b>79,281</b>
<b>Shareholders equity</b>				
Common stock (1,750.0 shares authorized; 386.0 shares issued and outstanding)		390	20,970	(390) 20,970
Additional paid-in capital	11,135	6,501	(17,636)	
Retained earnings	6,408	1,067	20,531	(7,465) 20,541
Accumulated other comprehensive income	1,992	870	2,130	(2,862) 2,130
Treasury stock, at cost (361.4 shares)			(18,592)	(18,592)
<b>Total shareholders equity</b>	<b>19,535</b>	<b>8,828</b>	<b>25,039</b>	<b>(28,353) 25,049</b>
<b>Total liabilities and shareholders equity</b>	<b>\$ 69,835</b>	<b>\$ 32,113</b>	<b>\$ 30,735</b>	<b>(28,353) \$ 104,330</b>

(1) The Travelers Companies, Inc., excluding its subsidiaries.

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At December 31, 2011

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Assets</b>					
Fixed maturities, available for sale, at fair value (amortized cost \$59,994)	\$ 43,438	\$ 20,761	\$ 33	\$	\$ 64,232
Equity securities, available for sale, at fair value (cost \$414)	146	319	94		559
Real estate investments	33	832			865
Short-term securities	879	376	2,339		3,594
Other investments	2,446	1,004	1		3,451
<b>Total investments</b>	<b>46,942</b>	<b>23,292</b>	<b>2,467</b>		<b>72,701</b>
Cash	114	98	2		214
Investment income accrued	517	251			768
Premiums receivable	3,865	1,865			5,730
Reinsurance recoverables	7,372	3,783			11,155
Ceded unearned premiums	656	172			828
Deferred acquisition costs	1,536	250			1,786
Deferred taxes	(82)	(47)	136		7
Contractholder receivables	3,891	1,295			5,186
Goodwill	2,411	954			3,365
Other intangible assets	297	136			433
Investment in subsidiaries			27,565	(27,565)	
Other assets	1,983	52	367		2,402
<b>Total assets</b>	<b>\$ 69,502</b>	<b>\$ 32,101</b>	<b>\$ 30,537</b>	<b>\$ (27,565)</b>	<b>\$ 104,575</b>
<b>Liabilities</b>					
Claims and claim adjustment expense reserves	\$ 33,727	\$ 17,665	\$	\$	\$ 51,392
Unearned premium reserves	7,644	3,458			11,102
Contractholder payables	3,891	1,295			5,186
Payables for reinsurance premiums	178	211			389
Debt	1,190		5,415		6,605

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Other liabilities	3,910	859	655	5,424
<b>Total liabilities</b>	<b>50,540</b>	<b>23,488</b>	<b>6,070</b>	<b>80,098</b>
<b>Shareholders' equity</b>				
Common stock (1,750.0 shares authorized; 392.8 shares issued and outstanding)		390	20,732	(390) 20,732
Additional paid-in capital	11,135	6,501	(17,636)	
Retained earnings	5,900	882	19,569	(6,772) 19,579
Accumulated other comprehensive income	1,927	840	2,005	(2,767) 2,005
Treasury stock, at cost (349.0 shares)			(17,839)	(17,839)
<b>Total shareholders' equity</b>	<b>18,962</b>	<b>8,613</b>	<b>24,467</b>	<b>(27,565) 24,477</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 69,502</b>	<b>\$ 32,101</b>	<b>\$ 30,537</b>	<b>(27,565) \$ 104,575</b>

(1) The Travelers Companies, Inc., excluding its subsidiaries.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES, Continued

## CONSOLIDATING STATEMENT OF CASH FLOWS (Unaudited)

For the six months ended June 30, 2012

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Cash flows from operating activities</b>					
Net income	\$ 1,012	\$ 394	\$ 1,305	\$ (1,406)	\$ 1,305
Net adjustments to reconcile net income to net cash provided by operating activities	109	(283)	(560)	694	(40)
<b>Net cash provided by operating activities</b>	<b>1,121</b>	<b>111</b>	<b>745</b>	<b>(712)</b>	<b>1,265</b>
<b>Cash flows from investing activities</b>					
Proceeds from maturities of fixed maturities	2,817	1,350			4,167
Proceeds from sales of investments:					
Fixed maturities	368	173	1		542
Equity securities	15	7			22
Real estate		3			3
Other investments	297	89			386
Purchases of investments:					
Fixed maturities	(3,744)	(1,454)	(2)		(5,200)
Equity securities	(2)	(30)	(1)		(33)
Real estate		(58)			(58)
Other investments	(139)	(82)			(221)
Net sales (purchases) of short-term securities	(176)	115	428		367
Securities transactions in course of settlement	87	(10)			77
Other	(144)	11			(133)
<b>Net cash provided by (used in) investing activities</b>	<b>(621)</b>	<b>114</b>	<b>426</b>		<b>(81)</b>
<b>Cash flows from financing activities</b>					
Payment of debt			(258)		(258)
Dividends paid to shareholders			(341)		(341)
Issuance of common stock			170		170
employee share options			(707)		(707)



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Treasury shares acquired	share repurchase				
authorization					
Treasury shares acquired	net employee				
share-based compensation			(52)		(52)
Excess tax benefits from share-based	payment arrangements			19	19
Dividends paid to parent company		(504)	(208)		712
<b>Net cash used in financing activities</b>		(504)	(208)	(1,169)	712
Effect of exchange rate changes on cash			1		1
Net increase (decrease) in cash		(4)	18	2	16
Cash at beginning of year		114	98	2	214
<b>Cash at end of period</b>		\$ 110	\$ 116	\$ 4	\$ 230
<b>Supplemental disclosure of cash flow information</b>					
Income taxes paid (received)		\$ 286	\$ 113	\$ (103)	\$ 296
Interest paid		\$ 36	\$	\$ 155	\$ 191

(1) The Travelers Companies, Inc., excluding its subsidiaries.

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## THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

## 13. CONSOLIDATING FINANCIAL STATEMENTS OF THE TRAVELERS COMPANIES, INC. AND SUBSIDIARIES, Continued

## CONSOLIDATING STATEMENT OF CASH FLOWS (Unaudited)

For the six months ended June 30, 2011

(in millions)	TPC	Other Subsidiaries	Travelers (1)	Eliminations	Consolidated
<b>Cash flows from operating activities</b>					
Net income	\$ 456	\$ 43	\$ 475	\$ (499)	\$ 475
Net adjustments to reconcile net income to net cash provided by operating activities	355	99	(174)	146	426
<b>Net cash provided by operating activities</b>	<b>811</b>	<b>142</b>	<b>301</b>	<b>(353)</b>	<b>901</b>
<b>Cash flows from investing activities</b>					
Proceeds from maturities of fixed maturities	1,969	1,265			3,234
Proceeds from sales of investments:					
Fixed maturities	382	353	1		736
Equity securities	15	32			47
Other investments	183	102			285
Purchases of investments:					
Fixed maturities	(2,342)	(1,204)	(1)		(3,547)
Equity securities		(74)	(29)		(103)
Real estate investments	(24)	(11)			(35)
Other investments	(549)	(80)			(629)
Net sales (purchases) of short-term securities	(108)	(500)	1,205		597
Securities transactions in course of settlement	150	63			213
Other	(135)	(8)			(143)
<b>Net cash provided by (used in) investing activities</b>	<b>(459)</b>	<b>(62)</b>	<b>1,176</b>		<b>655</b>
<b>Cash flows from financing activities</b>					
Payment of debt		(8)			(8)
Dividends paid to shareholders			(329)		(329)
Issuance of common stock employee share options			245		245
Treasury shares acquired share repurchase authorization			(1,360)		(1,360)

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Treasury shares acquired net employee share-based compensation			(46)		(46)
Excess tax benefits from share-based payment arrangements			11		11
Dividends paid to parent company	(353)			353	
<b>Net cash used in financing activities</b>	<b>(353)</b>	<b>(8)</b>	<b>(1,479)</b>	<b>353</b>	<b>(1,487)</b>
Effect of exchange rate changes on cash		4			4
Net increase (decrease) in cash	(1)	76	(2)		73
Cash at beginning of year	86	110	4		200
<b>Cash at end of period</b>	<b>\$ 85</b>	<b>\$ 186</b>	<b>\$ 2</b>	<b>\$</b>	<b>\$ 273</b>
<b>Supplemental disclosure of cash flow information</b>					
Income taxes paid (received)	\$ 199	\$ 114	\$ (22)	\$	\$ 291
Interest paid	\$ 36	\$	\$ 155	\$	\$ 191

(1) The Travelers Companies, Inc., excluding its subsidiaries.

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**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following is a discussion and analysis of the Company's financial condition and results of operations.

**FINANCIAL HIGHLIGHTS**

**2012 Second Quarter Consolidated Results of Operations**

- Net income of \$499 million, or \$1.27 per share basic and \$1.26 per share diluted
- Net earned premiums of \$5.53 billion
- Catastrophe losses of \$549 million (\$357 million after-tax)
- Net favorable prior year reserve development of \$221 million (\$147 million after-tax)
- GAAP combined ratio of 100.5%
- Net investment income of \$738 million (\$589 million after-tax)
- Operating cash flows of \$451 million

**2012 Second Quarter Consolidated Financial Condition**

- Total investments of \$72.94 billion; fixed maturities and short-term securities comprised 93% of total investments
- Total assets of \$104.33 billion
- Total debt of \$6.35 billion, resulting in a debt-to-total capital ratio of 20.2% (22.3% excluding net unrealized investment gains, net of tax)
- Repurchased 5.6 million common shares for total cost of \$350 million under share repurchase authorization
- Shareholders' equity of \$25.05 billion
- Book value per common share of \$64.90, up 9% from June 30, 2011

- Holding company liquidity of \$1.98 billion

Table of Contents**CONSOLIDATED OVERVIEW****Consolidated Results of Operations**

(in millions, except ratio and per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenues</b>				
Premiums	\$ 5,529	\$ 5,503	\$ 11,052	\$ 10,874
Net investment income	738	758	1,478	1,537
Fee income	59	74	141	148
Net realized investment gains	4	19	14	39
Other revenues	29	34	66	68
<b>Total revenues</b>	<b>6,359</b>	<b>6,388</b>	<b>12,751</b>	<b>12,666</b>
<b>Claims and expenses</b>				
Claims and claim adjustment expenses	3,786	5,141	7,150	8,523
Amortization of deferred acquisition costs	976	970	1,947	1,918
General and administrative expenses	893	907	1,777	1,790
Interest expense	96	97	192	193
<b>Total claims and expenses</b>	<b>5,751</b>	<b>7,115</b>	<b>11,066</b>	<b>12,424</b>
<b>Income (loss) before income taxes</b>	<b>608</b>	<b>(727)</b>	<b>1,685</b>	<b>242</b>
Income tax expense (benefit)	109	(363)	380	(233)
<b>Net income (loss)</b>	<b>\$ 499</b>	<b>\$ (364)</b>	<b>\$ 1,305</b>	<b>\$ 475</b>
<b>Net income (loss) per share</b>				
Basic	\$ 1.27	\$ (0.88)	\$ 3.32	\$ 1.11
Diluted	\$ 1.26	\$ (0.88)	\$ 3.29	\$ 1.10
<b>GAAP combined ratio</b>				
Loss and loss adjustment expense ratio	68.1%	92.6%	64.1%	77.6%
Underwriting expense ratio	32.4	32.4	32.2	32.5
<b>GAAP combined ratio</b>	<b>100.5%</b>	<b>125.0%</b>	<b>96.3%</b>	<b>110.1%</b>
<b>Incremental impact of direct to consumer initiative on GAAP combined ratio</b>	<b>0.7%</b>	<b>0.9%</b>	<b>0.7%</b>	<b>1.0%</b>

The following discussions of the Company's net income (loss) and segment operating income (loss) are presented on an after-tax basis. Discussions of the components of net income (loss) and segment operating income (loss) are presented on a pretax basis, unless otherwise noted. Discussions of net income (loss) per common share are presented on a diluted basis.

*Overview*

Diluted net income per share in the second quarter of 2012 was \$1.26, compared with diluted net loss per share of \$(0.88) in the second quarter of 2011, reflecting net income in the second quarter of 2012 of \$499 million, compared with a net loss of \$(364) million in the same period of

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2011 and the favorable impact of common share repurchases. The improvement in net income in the second quarter of 2012 compared with the prior year quarter primarily reflected (i) a significant decline in catastrophe losses and, to a lesser extent, (ii) higher underwriting margins excluding catastrophe losses and prior year reserve development ( underlying underwriting margins ) primarily resulting from earned pricing that exceeded loss costs and (iii) an increase in net favorable prior year reserve development, partially offset by slightly lower net investment income. Catastrophe losses in the second quarter of 2012 were \$549 million, compared with \$1.67 billion in the same period of 2011. Net favorable prior year reserve development in the second quarter of 2012 was \$221 million, compared with \$168 million in the same period of 2011.

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Diluted net income per share in the first six months of 2012 was \$3.29, compared with diluted net income per share of \$1.10 in the same period of 2011, reflecting net income in the first six months of 2012 of \$1.31 billion, compared with net income of \$475 million in the same period of 2011 and the favorable impact of common share repurchases. The increase in net income primarily reflected the same factors discussed above. Catastrophe losses in the first six months of 2012 were \$717 million, compared with \$1.85 billion in the same period of 2011. Net favorable prior year reserve development in the first six months of 2012 was \$525 million, compared with \$405 million in the same period of 2011. In addition, net income in the first six months of 2011 reflected a \$104 million benefit resulting from the favorable resolution of various prior year tax matters recorded in the first quarter of 2011.

**Revenues***Earned Premiums*

Earned premiums in the second quarter of 2012 were \$5.53 billion, \$26 million or less than 1% higher than in the same period of 2011. Earned premiums in the first six months of 2012 were \$11.05 billion, \$178 million or 2% higher than in the same period of 2011. In the Business Insurance segment, earned premiums in the second quarter and first six months of 2012 increased by 2% and 3% over the respective periods of 2011. In the Financial, Professional & International Insurance segment, earned premiums in the second quarter and first six months of 2012 both decreased by 5% from the same 2011 periods. In the Personal Insurance segment, earned premiums in the second quarter and first six months of 2012 increased by 1% and 2% over the respective periods of 2011. Factors contributing to the changes in earned premiums in each segment are discussed in more detail in the segment discussions that follow.

*Net Investment Income*

The following table sets forth information regarding the Company's investments.

(dollars in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Average investments (a)	\$ 69,623	\$ 70,476	\$ 69,555	\$ 70,659
Pretax net investment income	738	758	1,478	1,537
After-tax net investment income	589	606	1,182	1,228
Average pretax yield (b)	4.2%	4.3%	4.2%	4.4%
Average after-tax yield (b)	3.4%	3.4%	3.4%	3.5%

(a) Excludes net unrealized investment gains and losses, net of tax, and reflects cash, receivables for investment sales, payables on investment purchases and accrued investment income.

(b) Excludes net realized investment gains and losses and net unrealized investment gains and losses, net of tax.



Net investment income in the second quarter of 2012 was \$738 million, \$20 million or 3% lower than in the same period of 2011. Net investment income in the first six months of 2012 was \$1.48 billion, \$59 million or 4% lower than in the same period of 2011. Net investment income from fixed maturity investments in the second quarter and first six months of 2012 was \$611 million and \$1.23 billion, respectively, \$23 million and \$45 million lower, respectively, than in the same periods of 2011. The declines in both periods primarily resulted from lower long-term reinvestment yields available in the market. Net investment income generated by non-fixed maturity investments in the second quarter and first six months of 2012 was \$133 million and \$261 million, respectively, \$4 million higher and \$8 million lower, respectively, than in the same periods of 2011.

*Fee Income*

The National Accounts market in the Business Insurance segment is the primary source of the Company's fee-based business. The \$15 million and \$7 million decreases in fee income in the second quarter and first six months of 2012, respectively, compared with the same periods of 2011 are discussed in the Business Insurance segment discussion that follows.

Table of Contents*Net Realized Investment Gains*

The following table sets forth information regarding the Company's net realized investment gains.

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Net Realized Investment Gains</b>				
Other-than-temporary impairment losses:				
Total gains	\$ 11	\$ 5	\$ 11	\$ 7
Non-credit component of impairments recognized in accumulated other comprehensive income	(15)	(9)	(19)	(15)
Other-than-temporary impairment losses	(4)	(4)	(8)	(8)
Other net realized investment gains	8	23	22	47
<b>Net realized investment gains</b>	<b>\$ 4</b>	<b>\$ 19</b>	<b>\$ 14</b>	<b>\$ 39</b>

*Other Revenues*

Other revenues in the second quarter and first six months of both 2012 and 2011 primarily consisted of premium installment charges.

**Claims and Expenses***Claims and Claim Adjustment Expenses*

Claims and claim adjustment expenses in the second quarter of 2012 were \$3.79 billion, \$1.36 billion or 26% lower than in the same period of 2011. The decrease primarily reflected (i) the significant decline in catastrophe losses and, to a much lesser extent, (ii) lower levels of what the Company defines as large losses and non-catastrophe weather-related losses, and (iii) an increase in net favorable prior year reserve development, partially offset by the impact of loss cost trends. Catastrophe losses in the second quarters of 2012 and 2011 were \$549 million and \$1.67 billion, respectively. Catastrophe losses in the second quarter of 2012 primarily resulted from wind and hail storms in several regions of the United States. Catastrophe losses in the second quarter of 2011 resulted from multiple tornadoes and hail storms, primarily in the Midwest and Southeast regions of the United States. Net favorable prior year reserve development in the second quarters of 2012 and 2011 was \$221 million and \$168 million, respectively.

Claims and claim adjustment expenses in the first six months of 2012 were \$7.15 billion, \$1.37 billion or 16% lower than in the same period of 2011, primarily reflecting the same factors described above. Catastrophe losses in the first six months of 2012 and 2011 were \$717 million and \$1.85 billion, respectively. Catastrophe losses in the first six months of 2012 included the second quarter storms described above, as well as

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tornadoes and hail storms in the Midwest and Southeast regions of the United States in the first quarter of 2012. Catastrophe losses in the first six months of 2011 included the second quarter storms described above, as well severe winter storms throughout the United States in the first quarter of 2011. Net favorable prior year reserve development in the first six months of 2012 and 2011 was \$525 million and \$405 million, respectively. Factors contributing to net favorable prior year reserve development in each segment during these periods are discussed in more detail in the segment discussions that follow.

### *Amortization of Deferred Acquisition Costs*

The amortization of deferred acquisition costs in the second quarter of 2012 was \$976 million, \$6 million or 1% higher than in the same period of 2011. The amortization of deferred acquisition costs in the first six months of 2012 was \$1.95 billion, \$29 million or 2% higher than in the same 2011 period. The increases in both periods of 2012 were generally consistent with the increases in earned premiums.

### *General and Administrative Expenses*

General and administrative expenses in the second quarter of 2012 were \$893 million, \$14 million or 2% lower than in the same period of 2011. General and administrative expenses in the first six months of 2012 were \$1.78 billion, \$13 million or 1% lower than in the same period of 2011. General and administrative expenses are discussed in more detail in the segment discussions that follow.

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*Interest Expense*

Interest expense in the second quarter and first six months of 2012 was \$96 million and \$192 million, respectively, virtually level with the same periods of 2011.

*Income Taxes.* The Company's effective tax rates in the second quarter and first six months of 2012 were 18% and 23%, respectively, lower than the statutory rate of 35% primarily due to the impact of tax-exempt investment income on the calculation of the Company's income tax provision. The Company's income tax benefits of \$363 million and \$233 million in the second quarter and first six months of 2011, respectively, primarily reflected the pretax net loss in the second quarter of 2011, as well as the impact of tax-exempt investment income on the calculation of the Company's tax provision in both periods. In addition, the year-to-date income tax benefit in 2011 included the \$104 million benefit resulting from the favorable resolution of various prior year tax matters recorded in the first quarter of 2011.

**GAAP Combined Ratio**

The consolidated GAAP combined ratio of 100.5% in the second quarter of 2012 was 24.5 points lower than the consolidated GAAP combined ratio of 125.0% in the same period of 2011. The consolidated GAAP combined ratio of 96.3% in the first six months of 2012 was 13.8 points lower than the consolidated GAAP combined ratio of 110.1% in the same period of 2011.

The consolidated loss and loss adjustment expense ratio of 68.1% in the second quarter of 2012 was 24.5 points lower than the consolidated loss and loss adjustment expense ratio of 92.6% in the same period of 2011. Catastrophe losses accounted for 10.0 points and 30.3 points of the 2012 and 2011 second quarter loss and loss adjustment expense ratios, respectively. The 2012 and 2011 second quarter loss and loss adjustment expense ratios included 4.0 and 3.1 points of benefit from net favorable prior year reserve development, respectively. The 2012 second quarter loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development was 3.3 points lower than the 2011 ratio on the same basis, primarily reflecting earned pricing that exceeded loss cost trends, as well as lower levels of what the Company defines as large losses and non-catastrophe weather-related losses.

The consolidated loss and loss adjustment expense ratio of 64.1% in the first six months of 2012 was 13.5 points lower than the consolidated loss and loss adjustment expense ratio of 77.6% in the same period of 2011. Catastrophe losses accounted for 6.5 points and 17.1 points of the 2012 and 2011 six month loss and loss adjustment expense ratios, respectively. The 2012 and 2011 six month loss and loss adjustment expense ratios included 4.8 and 3.7 points of benefit from net favorable prior year reserve development, respectively. The 2012 six month loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development was 1.8 points lower than the 2011 ratio on the same basis, also reflecting the same factors discussed above for the second quarter of 2012.

The consolidated underwriting expense ratio of 32.4% for the second quarter of 2012 was level with the consolidated underwriting expense ratio in the same period of 2011. In the first six months of 2012, the consolidated underwriting expense ratio of 32.2% was 0.3 points lower than the consolidated underwriting expense ratio of 32.5% in the same 2011 period.

*Written Premiums*

Consolidated gross and net written premiums were as follows:

(in millions)	Gross Written Premiums					
	Three Months Ended June 30,			Six Months Ended June 30,		
	2012	2011		2012	2011	
Business Insurance	\$ 3,280	\$ 3,094		\$ 6,709	\$ 6,400	
Financial, Professional & International Insurance	882	910		1,673	1,720	
Personal Insurance	2,078	2,120		3,931	3,965	
<b>Total</b>	\$ 6,240	\$ 6,124		\$ 12,313	\$ 12,085	

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(in millions)	Net Written Premiums					
	Three Months Ended			Six Months Ended		
	2012	June 30, 2011	2012	June 30, 2011	2011	
Business Insurance	\$ 3,026	\$ 2,879	\$ 6,126	\$ 5,899		
Financial, Professional & International Insurance	840	879	1,444	1,503		
Personal Insurance	2,002	2,059	3,795	3,852		
<b>Total</b>	<b>\$ 5,868</b>	<b>\$ 5,817</b>	<b>\$ 11,365</b>	<b>\$ 11,254</b>		

Gross and net written premiums in the second quarter of 2012 increased by 2% and 1%, respectively, over the same period of 2011. Gross and net written premiums in the first six months of 2012 also increased by 2% and 1%, respectively, over the same period of 2011. Factors contributing to the changes in gross and net written premiums in each segment are discussed in more detail in the segment discussions that follow.

**RESULTS OF OPERATIONS BY SEGMENT****Business Insurance**

Results of the Company's Business Insurance segment were as follows:

(dollars in millions)	Three Months Ended			Six Months Ended		
	June 30,		June 30,			
	2012	2011	2012	2011	2011	
<b>Revenues</b>						
Earned premiums	\$ 2,860	\$ 2,802	\$ 5,736	\$ 5,547		
Net investment income	536	541	1,068	1,097		
Fee income	58	74	140	148		
Other revenues	8	10	22	19		
<b>Total revenues</b>	<b>\$ 3,462</b>	<b>\$ 3,427</b>	<b>\$ 6,966</b>	<b>\$ 6,811</b>		
<b>Total claims and expenses</b>	<b>\$ 3,018</b>	<b>\$ 3,528</b>	<b>\$ 5,692</b>	<b>\$ 6,218</b>		
<b>Operating income</b>	<b>\$ 362</b>	<b>\$ 11</b>	<b>\$ 974</b>	<b>\$ 615</b>		
Loss and loss adjustment expense ratio	71.0%	90.6%	64.4%	77.0%		
Underwriting expense ratio	32.0	32.3	31.9	32.0		
<b>GAAP combined ratio</b>	<b>103.0%</b>	<b>122.9%</b>	<b>96.3%</b>	<b>109.0%</b>		

*Overview*

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Operating income in the second quarter of 2012 was \$362 million, \$351 million higher than operating income of \$11 million in the same period of 2011. The increase was driven by a significant decline in (i) catastrophe losses and, to a lesser extent, (ii) higher underlying underwriting margins primarily resulting from earned pricing that exceeded loss cost trends, (iii) higher net favorable prior year reserve development and (iv) lower levels of what the Company defines as large losses, partially offset by lower net investment income. Catastrophe losses in the second quarter of 2012 were \$252 million, compared with \$697 million in the same period of 2011. Net favorable prior year reserve development was \$58 million in the second quarter of 2012, compared with \$27 million in the same 2011 period.

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Operating income in the first six months of 2012 was \$974 million, \$359 million or 58% higher than operating income of \$615 million in the same period of 2011, primarily reflecting the same factors described above. In addition, operating income in the first six months of 2011 included a \$76 million benefit in the first quarter of 2011 resulting from the favorable resolution of various prior year tax matters. Catastrophe losses in the first six months of 2012 were \$305 million, compared with \$809 million in the same period of 2011. Net favorable prior year reserve development in the first six months of 2012 was \$306 million, compared with \$170 million in the same period of 2011.

*Earned Premiums*

Earned premiums in the second quarter of 2012 were \$2.86 billion, \$58 million or 2% higher than in the same period of 2011. Earned premiums in the first six months of 2012 were \$5.74 billion, \$189 million or 3% higher than in the same period of 2011. The increases in both periods of 2012 primarily reflected the impact of an increase in net written premiums over the preceding twelve months, partially offset by the impact of a reduction in earned premiums resulting from net favorable prior year reserve development on certain retrospectively-rated business in National Accounts.

*Net Investment Income*

Net investment income in the second quarter of 2012 was \$536 million, \$5 million or 1% lower than in the same 2011 period. Net investment income in the first six months of 2012 was \$1.07 billion, \$29 million or 3% lower than in the same period of 2011. Refer to the Net Investment Income section of the Consolidated Results of Operations discussion herein for a description of the factors contributing to the decline in the Company's consolidated net investment income in the second quarter and first six months of 2012 compared with the same periods of 2011. In addition, refer to note 2 of notes to the Company's consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for a discussion of the Company's net investment income allocation methodology.

*Fee Income*

National Accounts is the primary source of fee income due to its service businesses, which include claim and loss prevention services to large companies that choose to self-insure a portion of their insurance risks, as well as claims and policy management services to workers compensation residual market pools. Fee income in the second quarter and first six months of 2012 decreased by \$16 million and \$8 million from the respective periods of 2011, reflecting the impact of net favorable prior year reserve development in National Accounts (since fees are principally based on a percentage of losses or number of claims serviced), which reduced fee income by \$26 million in both the second quarter and first six months of 2012, partially offset by higher serviced premium volume in workers' compensation residual market pools.

**Claims and Expenses**

*Claim and Claims Adjustment Expenses*



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Claims and claim adjustment expenses in the second quarter of 2012 were \$2.05 billion, \$530 million or 21% lower than in the same period of 2011, primarily reflecting (i) a significant decline in catastrophe losses and, to a lesser extent, (ii) higher net favorable prior year reserve development and (iii) lower levels of what the Company defines as large losses, partially offset by the impact of loss cost trends. Catastrophe losses in the second quarter of 2012 were \$252 million, compared with \$697 million in the same period of 2011. Net favorable prior year reserve development in the second quarter of 2012 was \$58 million, compared with \$27 million in the same period of 2011. Net favorable prior year reserve development in the second quarter of 2012 was concentrated in the workers' compensation product line, primarily driven by better than expected frequency and severity related to lifetime medical claims, managed care savings and better than expected loss development for accident years 2008 and prior. Net favorable prior year reserve development in the second quarter of 2012 also reflected better than expected loss development in the property product line related to catastrophe losses incurred in 2011 and lower than expected claim department expenses. These factors were partially offset by a \$90 million increase to environmental reserves, which is discussed in further detail in the Environmental Claims and Litigation section herein. Net favorable prior year reserve development in the second quarter of 2011 was driven by better than expected loss development in the general liability product line, which was concentrated in excess coverages for accident years 2008 and prior and reflected what the Company believes are favorable legal and judicial environments, partially offset by a \$76 million increase to environmental reserves, which is discussed in further detail in the Environmental Claims and Litigation section herein.

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Claims and claim adjustment expenses in the first six months of 2012 were \$3.76 billion, \$594 million or 14% lower than in the same 2011 period. The decrease primarily reflected the same factors discussed above. Catastrophe losses in the first six months of 2012 were \$305 million, compared with \$809 million in the same period of 2011. Net favorable prior year reserve development in the first six months of 2012 was \$306 million, compared with \$170 million in the same period of 2011. Net favorable prior year reserve development in the first six months of 2012 was driven by the same factors described above, and by better than expected loss development in the general liability product line for accident years 2004-2009, which reflected what the Company believes are more favorable legal and judicial environments than the Company previously expected. Net favorable prior year reserve development in the first six months of 2011 was driven by the same factors described above, as well as better than expected loss development in the property product line for the 2010 accident year in the Inland Marine business unit in Target Risk Underwriting.

*Amortization of Deferred Acquisition Costs*

The amortization of deferred acquisition costs in the second quarter of 2012 was \$465 million, \$8 million or 2% higher than in the same period of 2011. The amortization of deferred acquisition costs in the first six months of 2012 was \$932 million, \$31 million or 3% higher than in the same 2011 period. The increases in both periods of 2012 were consistent with the increases in earned premiums.

*General and Administrative Expenses*

General and administrative expenses in the second quarter of 2012 were \$504 million, \$12 million or 2% higher than in the same period of 2011. General and administrative expenses in the first six months of 2012 were \$1.00 billion, \$37 million or 4% higher than in the same period of 2011.

*GAAP Combined Ratio*

The GAAP combined ratio of 103.0% in the second quarter of 2012 was 19.9 points lower than the GAAP combined ratio of 122.9% in the same period of 2011. The GAAP combined ratio of 96.3% in the first six months of 2012 was 12.7 points lower than the GAAP combined ratio of 109.0% in the same period of 2011.

The loss and loss adjustment expense ratio of 71.0% in the second quarter of 2012 was 19.6 points lower than the loss and loss adjustment expense ratio of 90.6% in the same period of 2011. Catastrophe losses in the second quarters of 2012 and 2011 accounted for 8.8 points and 24.9 points, respectively, of the loss and loss adjustment expense ratio. Net favorable prior year reserve development in the second quarters of 2012 and 2011 provided 2.0 points and 1.0 points of benefit, respectively, to the loss and loss adjustment expense ratio. The 2012 second quarter loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development was 2.5 points lower than the 2011 ratio on the same basis, primarily reflecting earned pricing that exceeded loss cost trends and lower levels of what the Company defines as large losses.

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The loss and loss adjustment expense ratio of 64.4% in the first six months of 2012 was 12.6 points lower than the loss and loss adjustment expense ratio of 77.0% in the same period of 2011. Catastrophe losses in the first six months of 2012 and 2011 accounted for 5.3 points and 14.6 points, respectively, of the loss and loss adjustment expense ratio. Net favorable prior year reserve development in the first six months of 2012 and 2011 provided 5.3 points and 3.1 points of benefit, respectively, to the loss and loss adjustment expense ratio. The loss and loss adjustment expense ratio in the first six months of 2012 excluding catastrophe losses and prior year reserve development was 1.1 points lower than the 2011 ratio on the same basis, primarily reflecting earned pricing that exceeded loss cost trends and lower levels of what the Company defines as large losses.

The underwriting expense ratio of 32.0% for the second quarter of 2012 was 0.3 points lower than the underwriting expense ratio of 32.3% in the same period of 2011. In the first six months of 2012, the underwriting expense ratio of 31.9% was 0.1 points lower than the underwriting expense ratio of 32.0% in the same 2011 period. In both periods of 2012, the impact of higher earned premiums was largely offset by the impact of higher general and administrative expenses.

Table of Contents*Written Premiums*

The Business Insurance segment's gross and net written premiums by market were as follows:

(in millions)	Gross Written Premiums				
	Three Months Ended June 30,		Six Months Ended June 30,		
	2012	2011	2012	2011	2011
Select Accounts	\$ 730	\$ 743	\$ 1,461	\$ 1,481	
Commercial Accounts	748	689	1,652	1,556	
National Accounts	328	253	700	569	
Industry-Focused Underwriting	646	588	1,331	1,254	
Target Risk Underwriting	591	577	1,118	1,082	
Specialized Distribution	243	246	451	455	
<b>Total Business Insurance Core</b>	<b>3,286</b>	<b>3,096</b>	<b>6,713</b>	<b>6,397</b>	
Business Insurance Other	(6)	(2)	(4)	3	
<b>Total Business Insurance</b>	<b>\$ 3,280</b>	<b>\$ 3,094</b>	<b>\$ 6,709</b>	<b>\$ 6,400</b>	

(in millions)	Net Written Premiums				
	Three Months Ended June 30,		Six Months Ended June 30,		
	2012	2011	2012	2011	2011
Select Accounts	\$ 721	\$ 738	\$ 1,439	\$ 1,470	
Commercial Accounts	717	659	1,578	1,481	
National Accounts	226	188	461	399	
Industry-Focused Underwriting	636	579	1,284	1,207	
Target Risk Underwriting	486	468	915	881	
Specialized Distribution	242	246	450	455	
<b>Total Business Insurance Core</b>	<b>3,028</b>	<b>2,878</b>	<b>6,127</b>	<b>5,893</b>	
Business Insurance Other	(2)	1	(1)	6	
<b>Total Business Insurance</b>	<b>\$ 3,026</b>	<b>\$ 2,879</b>	<b>\$ 6,126</b>	<b>\$ 5,899</b>	

In Business Insurance Core, gross and net written premiums in the second quarter of 2012 increased by 6% and 5%, respectively, over the same period of 2011. Gross and net written premiums in the first six months of 2012 increased by 5% and 4%, respectively, over the same period of 2011. The increases in gross and net written premiums in the second quarter and first six months of 2012 were concentrated in Commercial Accounts, Industry-Focused Underwriting and National Accounts, and were largely driven by positive audit premium adjustments (which were higher than in the same periods of 2011) and rate increases. Overall business retention rates remained strong in the second quarter and first six months of 2012 but declined modestly from the respective periods of 2011. Renewal premium changes comprising both renewal rate changes and insured exposure growth remained positive in the second quarter and first six months of 2012 and increased over the respective periods of 2011. New business levels declined from the second quarter and first six months of 2011.

*Select Accounts.* Net written premiums of \$721 million in the second quarter of 2012 declined by 2% from the same period of 2011. Net written premiums of \$1.44 billion in the first six months of 2012 also declined by 2% from the same period of 2011. Business retention rates in the second quarter and first six months of 2012 remained strong but were lower than in the same periods of 2011. Renewal premium changes remained positive in the second quarter and first six months of 2012 and increased over the same periods of 2011, primarily due to renewal rate increases. New business volume in the second quarter and first six months of 2012 declined from the same periods of 2011.



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*Commercial Accounts.* Net written premiums of \$717 million in the second quarter of 2012 increased by 9% over the same period of 2011. Net written premiums of \$1.58 billion in the first six months of 2012 increased by 7% over the same period of 2011. Net written premiums in the second quarter and first six months of 2012 were favorably impacted by positive audit premium adjustments. Business retention rates remained strong but were lower than in the second quarter and first six months of 2011. Renewal premium changes remained positive in the second quarter and first six months of 2012 and increased over the same periods of 2011, primarily due to renewal rate increases. New business volumes declined compared with the second quarter and first six months of 2011.

*National Accounts.* Net written premiums of \$226 million in the second quarter of 2012 increased by 20% over the same period of 2011. Net written premiums of \$461 million in the first six months of 2012 increased by 16% over the same period of 2011. Business retention rates remained high in the second quarter and first six months of 2012 and increased over the same periods of 2011. Renewal premium changes were positive and increased over the second quarter and first six months of 2011, driven by payroll exposure growth. New business volumes also increased over the second quarter and first six months of 2011. In addition, the re-population of workers' compensation residual market pools contributed to premium growth in both periods of 2012.

*Industry-Focused Underwriting.* Net written premiums of \$636 million in the second quarter of 2012 increased by 10% over the same period of 2011. Net written premiums of \$1.28 billion in the first six months of 2012 increased by 6% over the same period of 2011. Premium increases in both periods of 2012 were driven by growth in the Construction and Oil & Gas business units.

*Target Risk Underwriting.* Net written premiums of \$486 million in the second quarter of 2012 increased by 4% over the same period of 2011. Net written premiums of \$915 million in the first six months of 2012 also increased by 4% over the same period of 2011. Premium growth in the second quarter of 2012 was concentrated in the National Property business unit, while premium growth in the first six months of 2012 was concentrated in the National Property and Excess Casualty business units.

*Specialized Distribution.* Net written premiums of \$242 million in the second quarter of 2012 decreased by 2% from the same period of 2011. Net written premiums of \$450 million in the first six months of 2012 also decreased by 1% from the same period of 2011.

**Financial, Professional & International Insurance**

Results of the Company's Financial, Professional & International Insurance segment were as follows:

(dollars in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenues</b>				
Earned premiums	\$ 766	\$ 810	\$ 1,503	\$ 1,583
Net investment income	99	105	203	211
Fee income	1		1	
Other revenues	5	6	13	13

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<b>Total revenues</b>	\$	<b>871</b>	\$	921	\$	<b>1,720</b>	\$	1,807
<b>Total claims and expenses</b>	\$	<b>616</b>	\$	690	\$	<b>1,265</b>	\$	1,430
<b>Operating income</b>	\$	<b>182</b>	\$	164	\$	<b>331</b>	\$	284
Loss and loss adjustment expense ratio		<b>39.1%</b>		46.2%		<b>42.5%</b>		50.8%
Underwriting expense ratio		<b>40.9</b>		38.6		<b>41.3</b>		39.1
<b>GAAP combined ratio</b>		<b>80.0%</b>		84.8%		<b>83.8%</b>		89.9%

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*Overview*

Operating income in the second quarter of 2012 was \$182 million, \$18 million or 11% higher than operating income of \$164 million in the second quarter of 2011, primarily reflecting higher underlying underwriting margins resulting from (i) earned pricing that exceeded loss cost trends, as well as lower levels of (ii) what the Company defines as large losses, (iii) non-catastrophe weather-related losses and (iv) catastrophe losses, partially offset by the impact of lower business volumes and higher general and administrative expenses. Catastrophe losses in the second quarter of 2012 were \$4 million, compared with \$14 million in the same 2011 period. Net favorable prior year reserve development in the second quarter of 2012 was \$96 million, compared with \$96 million in the same 2011 period.

Operating income in the first six months of 2012 was \$331 million, \$47 million or 17% higher than operating income of \$284 million in the same period of 2011, primarily reflecting the same factors described above. In addition, operating income in the first six months of 2011 included a \$14 million benefit resulting from the favorable resolution of various prior year tax matters. Catastrophe losses in the first six months of 2012 were \$4 million, compared with \$35 million in the same period of 2011. Net favorable prior year reserve development in the first six months of 2012 was \$142 million, compared with \$135 million in the same period of 2011.

*Earned Premiums*

Earned premiums in the second quarter of 2012 were \$766 million, \$44 million or 5% lower than in the same period of 2011. Earned premiums in the first six months of 2012 were \$1.50 billion, \$80 million or 5% lower than in the same period of 2011. The declines in both periods of 2012 primarily reflected the impact of a decrease in net written premiums over the preceding twelve months and, to a lesser extent, the impact of foreign currency rates of exchange.

*Net Investment Income*

Net investment income in the second quarter of 2012 was \$99 million, \$6 million or 6% lower than in the same period of 2011. Net investment income in the first six months of 2012 was \$203 million, \$8 million or 4% lower than in the same period of 2011. Included in the Financial, Professional & International Insurance segment are certain legal entities whose invested assets and related net investment income are reported exclusively in this segment and not allocated among all business segments. Refer to the *Net Investment Income* section of *Consolidated Results of Operations* herein for a discussion of the change in the Company's consolidated net investment income in the second quarter and first six months of 2012 as compared with the same periods of 2011. In addition, refer to note 2 of notes to the Company's consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for a discussion of the Company's net investment income allocation methodology.

**Claims and Expenses**

*Claims and Claim Adjustment Expenses*



Claims and claim adjustment expenses in the second quarter of 2012 were \$302 million, \$76 million or 20% lower than in the same period of 2011, primarily reflecting lower levels of (i) what the Company defines as large losses, (ii) non-catastrophe weather-related losses, (iii) catastrophe losses, and (iv) claims and claim adjustment expenses related to lower business volumes. Catastrophe losses in the second quarter of 2012 were \$4 million, compared with \$14 million in the same period of 2011. Net favorable prior year reserve development in the second quarters of both 2012 and 2011 was \$96 million. Both Bond & Financial Products and International contributed to the net favorable prior year reserve development in the second quarter of 2012. In Bond & Financial Products, net favorable prior year reserve development primarily reflected better than expected results for the surety business for accident years 2008-2010, and better than expected results for the management liability business for accident years 2007 and prior. In International, net favorable development primarily reflected better than expected loss development in the Company's operation at Lloyd's in the marine and aviation business units across multiple accident years. Net favorable prior year reserve development in the second quarter of 2011 was concentrated in Bond & Financial Products and primarily reflected better than expected results for accident years 2008 and prior for the contract surety business, and for accident years 2007 and prior for the public company directors & officers line of business. Several product lines throughout the International group's operations also experienced net favorable prior year development for recent accident years in the second quarter of 2011.

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Claims and claim adjustment expenses in the first six months of 2012 were \$643 million, \$168 million or 21% lower than in the same 2011 period, primarily reflecting the same factors described above. Catastrophe losses in the first six months of 2012 were \$4 million, compared with \$35 million in the same period of 2011. Catastrophe losses in the first six months of 2011 included losses from an earthquake in Japan, as well as severe wind and hail storms throughout the United States. Net favorable prior year reserve development in the first six months of 2012 was \$142 million and was driven by the factors described above for the second quarter, as well as net favorable prior year reserve development in the first quarter of 2012 in both Bond & Financial Products and International. In Bond & Financial Products, net favorable prior year reserve development in the first quarter of 2012 primarily reflected better than expected results for the 2006 – 2008 accident years for the contract surety business. In International, net favorable prior year reserve development in the first quarter of 2012 reflected better than expected loss development in Canada, primarily in the surety and property lines of business for recent accident years and better than expected development in the Company's operation at Lloyd's in the marine and accident and special risks business units for recent accident years. Net favorable prior year reserve development in the first six months of 2011 was \$135 million, driven by the factors described above for the second quarter, as well as net favorable prior year reserve development in the first quarter of 2011 that was concentrated in Bond & Financial Products and primarily reflected better than expected results for accident years 2004 and prior for fidelity and surety coverages, including favorable loss development related to one large commercial surety claim.

*Amortization of Deferred Acquisition Expenses*

The amortization of deferred acquisition costs in the second quarter of 2012 was \$149 million, \$3 million or 2% lower than in the same period of 2011. The amortization of deferred acquisition costs in the first six months of 2012 was \$292 million, \$7 million or 2% lower than in the same 2011 period. The decreases in both periods of 2012 were generally consistent with the decrease in earned premiums.

*General and Administrative Expenses*

General and administrative expenses in the second quarter of 2012 were \$165 million, \$5 million or 3% higher than in the same period of 2011. General and administrative expenses in the first six months of 2012 were \$330 million, \$10 million or 3% higher than in the same period of 2011. The increases in both periods of 2012 primarily reflected an increase in technology-related costs to enhance operations and support future business growth.

*GAAP Combined Ratio*

The GAAP combined ratio of 80.0% in the second quarter of 2012 was 4.8 points lower than the GAAP combined ratio of 84.8% in the same period of 2011. The GAAP combined ratio of 83.8% in the first six months of 2012 was 6.1 points lower than the GAAP combined ratio of 89.9% in the same period of 2011.

The loss and loss adjustment expense ratio of 39.1% in the second quarter of 2012 was 7.1 points lower than the loss and loss adjustment expense ratio of 46.2% in the same period of 2011. Catastrophe losses in the second quarters of 2012 and 2011 accounted for 0.4 points and 1.7 points, respectively, of the loss and loss adjustment expense ratio. The 2012 and 2011 second quarter ratios included 12.5 points and 11.7 points of benefit, respectively, from net favorable prior year reserve development. The 2012 second quarter loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development was 5.0 points lower than the 2011 ratio on the same basis, reflecting the

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impact of earned pricing that exceeded loss cost trends, as well as lower levels of what the Company defines as large losses and non-catastrophe weather-related losses.

The loss and loss adjustment expense ratio of 42.5% in the first six months of 2012 was 8.3 points lower than the loss and loss adjustment expense ratio of 50.8% in the same period of 2011. Catastrophe losses in the first six months of 2012 and 2011 accounted for 0.2 points and 2.2 points, respectively, of the loss and loss adjustment expense ratio. The 2012 and 2011 year-to-date ratios included 9.4 points and 8.6 points of benefit, respectively, from net favorable prior year reserve development. The loss and loss adjustment expense ratio in the first six months of 2012 excluding catastrophe losses and prior year reserve development was 5.5 points lower than the 2011 ratio on the same basis, also reflecting the same factors discussed above for the second quarter of 2012.

The underwriting expense ratio of 40.9% in the second quarter of 2012 was 2.3 points higher than the underwriting expense ratio of 38.6% in the same period of 2011. In the first six months of 2012, the underwriting expense ratio of 41.3% was 2.2 points higher than the underwriting expense ratio of 39.1% in the same period of 2011. The increase in both periods of 2012 primarily reflected a decline in earned premiums and, to a lesser extent, an increase in general and administrative expenses.

Table of Contents*Written Premiums*

The Financial, Professional & International Insurance segment's gross and net written premiums by market were as follows:

(in millions)	Gross Written Premiums							
	Three Months Ended			Six Months Ended				
	2012	June 30,	2011	2012	June 30,	2011		
Bond & Financial Products	\$	525	\$	519	\$	1,010	\$	1,027
International		357		391		663		693
<b>Total Financial, Professional &amp; International Insurance</b>	<b>\$</b>	<b>882</b>	<b>\$</b>	<b>910</b>	<b>\$</b>	<b>1,673</b>	<b>\$</b>	<b>1,720</b>

(in millions)	Net Written Premiums							
	Three Months Ended			Six Months Ended				
	2012	June 30,	2011	2012	June 30,	2011		
Bond & Financial Products	\$	524	\$	533	\$	881	\$	902
International		316		346		563		601
<b>Total Financial, Professional &amp; International Insurance</b>	<b>\$</b>	<b>840</b>	<b>\$</b>	<b>879</b>	<b>\$</b>	<b>1,444</b>	<b>\$</b>	<b>1,503</b>

The Financial, Professional & International Insurance segment's gross and net written premiums in the second quarter of 2012 decreased by 3% and 4%, respectively, from the same period of 2011. In the first six months of 2012, gross and net written premiums also decreased by 3% and 4%, respectively, from the same period of 2011.

Net written premiums in Bond & Financial Products in the second quarter of 2012 were \$524 million, \$9 million or 2% lower than in the same period of 2011. Net written premiums in the first six months of 2012 were \$881 million, \$21 million or 2% lower than in the same period of 2011. The decreases in both periods of 2012 were primarily driven by the continued slowdown in construction spending and the timing of certain reinsurance transactions, partially offset by growth in management liability business volume. Excluding the surety line of business, for which the following are not relevant measures, business retention rates in the second quarter and first six months of 2012 remained strong and were higher than in the respective periods of 2011. Renewal premium changes in the second quarter and first six months of 2012 remained positive and were higher than in the respective periods of 2011, primarily driven by positive renewal rate changes. New business volume in the second quarter and first six months of 2012 also increased over the same periods of 2011.

Net written premiums in International in the second quarter of 2012 were \$316 million, \$30 million or 9% lower than in the same period of 2011. Net written premiums in the first six months of 2012 were \$563 million, \$38 million or 6% lower than in the same period of 2011. The decreases in both periods of 2012 largely reflected the impact of the Company's withdrawal from personal insurance business in the Republic of Ireland and the impact of foreign currency rates of exchange. Excluding the surety line of business, for which the following are not relevant measures, business retention rates in the second quarter and first six months of 2012 were strong and higher than in the respective periods of 2011. Renewal premium changes in the second quarter of 2012 were positive and higher than in the same period of 2011, reflecting continued

positive renewal rate changes combined with a smaller decline in insured exposures. Renewal premium changes in the first six months of 2012 were slightly positive and slightly higher than in the same period of 2011, as positive renewal rate changes were largely offset by a decline in insured exposures. New business volume in the second quarter and first six months of 2012 declined compared with the same periods of 2011.

Table of Contents**Personal Insurance**

Results of the Company's Personal Insurance segment were as follows:

(dollars in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<b>Revenues</b>				
Earned premiums	\$ 1,903	\$ 1,891	\$ 3,813	\$ 3,744
Net investment income	103	112	207	229
Other revenues	16	18	35	36
<b>Total revenues</b>	<b>\$ 2,022</b>	<b>\$ 2,021</b>	<b>\$ 4,055</b>	<b>\$ 4,009</b>
<b>Total claims and expenses</b>	<b>\$ 2,016</b>	<b>\$ 2,770</b>	<b>\$ 3,905</b>	<b>\$ 4,538</b>
<b>Operating income (loss)</b>	<b>\$ 17</b>	<b>\$ (471)</b>	<b>\$ 125</b>	<b>\$ (301)</b>
Loss and loss adjustment expense ratio				
	75.4%	115.6%	72.1%	89.8%
Underwriting expense ratio				
	29.4	29.9	29.2	30.3
<b>GAAP combined ratio</b>	<b>104.8%</b>	<b>145.5%</b>	<b>101.3%</b>	<b>120.1%</b>
<b>Incremental impact of direct to consumer initiative on GAAP combined ratio</b>				
	1.9%	2.3%	2.0%	2.6%

*Overview*

Operating income in the second quarter of 2012 was \$17 million, compared with an operating loss of \$(471) million in the same period of 2011. The improvement over the prior year quarter reflected (i) a significant decline in catastrophe losses and, to a lesser extent, (ii) lower non-catastrophe weather-related losses and fire-related losses, and (iii) an increase in net favorable prior year reserve development, partially offset by lower net investment income. Catastrophe losses in the second quarter of 2012 were \$293 million, compared with \$957 million in the same 2011 period. Net favorable prior year reserve development in the second quarter of 2012 was \$67 million, compared with \$45 million in the same 2011 period.

Operating income in the first six months of 2012 was \$125 million, compared with an operating loss of \$(301) million in the same 2011 period. The improvement was driven by the same factors described above, except that net favorable prior year reserve development in the first six months of 2012 was lower than in the same period of 2011. In addition, operating income in the first six months of 2011 included the impact of a \$10 million benefit in the first quarter of 2011 resulting from the favorable resolution of various prior year tax matters. Catastrophe losses in the first six months of 2012 were \$408 million, compared with \$1.01 billion in the same period of 2011. Net favorable prior year reserve development in the first six months of 2012 was \$77 million, compared with \$100 million in the same period of 2011.

*Earned Premiums*

Earned premiums in the second quarter of 2012 were \$1.90 billion, \$12 million or 1% higher than in the same period of 2011. Earned premiums in the first six months of 2012 were \$3.81 billion, \$69 million or 2% higher than in the same period of 2011. The increases in both periods of 2012 reflected growth in net written premiums over the preceding twelve months.

*Net Investment Income*

Net investment income in the second quarter of 2012 was \$103 million, \$9 million or 8% lower than in the same period of 2011. Net investment income in the first six months of 2012 was \$207 million, \$22 million or 10% lower than in the same period of 2011. Refer to the Net Investment Income section of the Consolidated Results of Operations discussion herein for a description of the factors contributing to the decline in the Company's consolidated net investment income in the second quarter and first six months of 2012 compared with the same periods of 2011. In addition, refer to note 2 of notes to the Company's consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for a discussion of the Company's net investment income allocation methodology.

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**Claims and Expenses**

*Claims and Claim Adjustment Expenses*

Claims and claim adjustment expenses in the second quarter of 2012 were \$1.43 billion, \$749 million or 34% lower than in the same period of 2011. The decrease primarily reflected (i) a significant decline in catastrophe losses and, to a lesser extent, lower (ii) non-catastrophe weather-related losses and fire-related losses, and (iii) higher net favorable prior year reserve development, partially offset by the impact of loss cost trends. Catastrophe losses in the second quarter of 2012 were \$293 million, compared with \$957 million in the same period of 2011. Net favorable prior year reserve development in the second quarter of 2012 was \$67 million, compared with \$45 million in the same period of 2011. Net favorable prior year reserve development in the second quarter of 2012 was primarily driven by better than expected development related to catastrophe losses incurred in 2011, as well as favorable loss development in the 2007-2011 accident years for the umbrella line of business in the Homeowners and Other product line. The 2011 total was driven by better than expected loss development related to catastrophe losses incurred in the first half of 2010, as well as favorable loss development in the 2006-2008 accident years for the umbrella line of business in the Homeowners and Other product line.

Claims and claim adjustment expenses in the first six months of 2012 were \$2.75 billion, \$611 million or 18% lower than in the same period of 2011, primarily reflecting the same factors described above, except that net favorable prior year reserve development in the first six months of 2012 was lower than in the same period of 2011. Catastrophe losses in the first six months of 2012 and 2011 were \$408 million and \$1.01 billion, respectively. Net favorable prior year reserve development in the first six months of 2012 and 2011 was \$77 million and \$100 million, respectively, driven by the same factors described above.

*Amortization of Deferred Acquisition Costs*

The amortization of deferred acquisition costs in the second quarter of 2012 was \$362 million, virtually level with the same period of 2011. The amortization of deferred acquisition costs in the first six months of 2012 was \$723 million, \$5 million or 1% higher than in the same 2011 period. The changes in both periods of 2012 were less than the increases in earned premiums for both periods, primarily reflecting lower fixed-value commission expense and growth in the Company's direct to consumer business (for which no commission expense is incurred).

*General and Administrative Expenses*

General and administrative expenses in the second quarter of 2012 were \$219 million, \$6 million or 3% lower than in the same period of 2011. General and administrative expenses in the first six months of 2012 were \$433 million, \$27 million, or 6%, lower than in the same period of 2011. The decreases in both periods of 2012 were primarily driven by the timing of advertising and other costs associated with the Company's direct to consumer business.

*GAAP Combined Ratio*



The GAAP combined ratio of 104.8% in the second quarter of 2012 was 40.7 points lower than the GAAP combined ratio of 145.5% in the same period of 2011. The GAAP combined ratio of 101.3% in the first six months of 2012 was 18.8 points lower than the GAAP combined ratio of 120.1% in the same period of 2011.

The loss and loss adjustment expense ratio of 75.4% in the second quarter of 2012 was 40.2 points lower than the loss and loss adjustment expense ratio of 115.6% in the same period of 2011. Catastrophe losses accounted for 15.3 points and 50.7 points of the loss and loss adjustment expense ratios in the second quarters of 2012 and 2011, respectively. The loss and loss adjustment expense ratio for the second quarters of 2012 and 2011 included 3.5 points and 2.4 points of benefit, respectively, from net favorable prior year reserve development. The 2012 second quarter loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development was 3.7 points lower than the 2011 ratio on the same basis, reflecting declines in non-catastrophe weather-related losses and fire-related losses.

The loss and loss adjustment expense ratio of 72.1% in the first six months of 2012 was 17.7 points lower than the loss and loss adjustment expense ratio of 89.8% in the same period of 2011. Catastrophe losses accounted for 10.7 points and 27.0 points of the loss and loss adjustment expense ratios in the first six months of 2012 and 2011, respectively. The loss and loss adjustment expense ratio for the first six months of 2012 and 2011 included 2.1 points and 2.7 points of benefit, respectively, from net favorable prior year reserve development. The 2012 six-month loss and loss adjustment expense ratio excluding catastrophe losses and prior year reserve development was 2.0 points lower than the 2011 ratio on the same basis, also reflecting the same factors discussed above for the second quarter of 2012.

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The underwriting expense ratio of 29.4% for the second quarter of 2012 was 0.5 points lower than the underwriting expense ratio of 29.9% in the same period of 2011. In the first six months of 2012, the underwriting expense ratio of 29.2% was 1.1 points lower than the underwriting expense ratio of 30.3% in the same 2011 period. The decreases in both periods of 2012 reflected growth in earned premiums and decreases in general and administrative expenses, primarily driven by the timing of advertising and other costs associated with the Company's direct to consumer business.

*Agency Written Premiums*

Personal Insurance's gross and net written premiums by product line were as follows for its Agency business, which comprises business written through agents, brokers and other intermediaries and represents almost all of the Personal Insurance segment's gross and net written premiums:

(in millions)	Gross Written Premiums							
	Three Months Ended			Six Months Ended				
	2012	June 30,	2011	2012	June 30,	2011		
Agency Automobile	\$	903	\$	952	\$	1,807	\$	1,875
Agency Homeowners and Other		1,135		1,136		2,047		2,027
<b>Total Agency Personal Insurance</b>	<b>\$</b>	<b>2,038</b>	<b>\$</b>	<b>2,088</b>	<b>\$</b>	<b>3,854</b>	<b>\$</b>	<b>3,902</b>

Agency Automobile	\$	899	\$	948	\$	1,799	\$	1,866
<b>Total Agency Personal Insurance</b>	<b>\$</b>	<b>1,963</b>	<b>\$</b>	<b>2,026</b>	<b>\$</b>	<b>3,718</b>	<b>\$</b>	<b>3,789</b>

Gross agency written premiums in the second quarter and first six months of 2012 were 2% and 1% lower than in the respective periods of 2011. Net agency written premiums in the second quarter and first six months of 2012 were 3% and 2% lower than in the respective periods of 2011.

In the Agency Automobile line of business, net written premiums in the second quarter and first six months of 2012 were 5% and 4% lower, respectively, than in the same periods of 2011. Business retention rates remained strong, while new business levels in the second quarter and first six months of 2012 declined from the same periods of 2011. Renewal premium changes remained positive in the second quarter and first six months of 2012 and increased over the same periods of 2011.

In the Agency Homeowners and Other line of business, net written premiums in the second quarter of 2012 were 1% lower than in the same period of 2011. Net written premiums in the first six months of 2012 were virtually level with the same period of 2011. Adjusting for the impact

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of the written premiums ceded related to the Company's new catastrophe bond program discussed in the Catastrophe Reinsurance Coverage section herein, net written premiums in the second quarter and first six months of 2012 were level with and slightly higher than the respective periods of 2011. Business retention rates remained strong, while new business levels in the second quarter and first six months of 2012 declined from the same periods of 2011. Renewal premium changes remained positive in the second quarter and first six months of 2012 and increased over the same periods of 2011.

For its Agency business, the Personal Insurance segment had approximately 7.5 million and 7.7 million active policies at June 30, 2012 and 2011, respectively.

In its direct to consumer business, net written premiums in the second quarter and first six months of 2012 were \$39 million and \$77 million, respectively, 18% and 22% higher than in the respective periods of 2011. Active policies were 154,000 at June 30, 2012, an increase of 27% over the same date in 2011.

Table of Contents**Interest Expense and Other**

Operating loss	\$	(66)	\$	(81)	\$	(134)	\$	(149)
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The operating losses for Interest Expense and Other in the second quarter and first six months of 2012 were both \$15 million lower than in the same periods of 2011. After-tax interest expense in the second quarter and first six months of both 2012 and 2011 was \$63 million and \$125 million, respectively.

**ASBESTOS CLAIMS AND LITIGATION**

The Company believes that the property and casualty insurance industry has suffered from court decisions and other trends that have expanded insurance coverage for asbestos claims far beyond the original intent of insurers and policyholders. The Company continues to receive a significant number of asbestos claims from the Company's policyholders (which includes others seeking coverage under a policy), including claims against the Company's policyholders by individuals who do not appear to be impaired by asbestos exposure. Factors underlying these claim filings include intensive advertising by lawyers seeking asbestos claimants and the focus by plaintiffs on previously peripheral defendants. The focus on these defendants is primarily the result of the number of traditional asbestos defendants who have sought bankruptcy protection in previous years. In addition to contributing to the overall number of claims, bankruptcy proceedings may increase the volatility of asbestos-related losses by initially delaying the reporting of claims and later by significantly accelerating and increasing loss payments by insurers, including the Company. The bankruptcy of many traditional defendants has also caused increased settlement demands against those policyholders who are not in bankruptcy but that remain in the tort system. Currently, in many jurisdictions, those who allege very serious injury and who can present credible medical evidence of their injuries are receiving priority trial settings in the courts, while those who have not shown any credible disease manifestation are having their hearing dates delayed or placed on an inactive docket. This trend of prioritizing claims involving credible evidence of injuries, along with the focus on previously peripheral defendants, contributes to the claims and claim adjustment expense payments experienced by the Company. The Company's asbestos-related claims and claim adjustment expense experience also has been impacted by the unavailability of other insurance sources potentially available to policyholders, whether through exhaustion of policy limits or through the insolvency of other participating insurers.

The Company continues to be involved in coverage litigation concerning a number of policyholders, some of whom have filed for bankruptcy, who in some instances have asserted that all or a portion of their asbestos-related claims are not subject to aggregate limits on coverage. In these instances, policyholders also may assert that each individual bodily injury claim should be treated as a separate occurrence under the policy. It is difficult to predict whether these policyholders will be successful on both issues. To the extent both issues are resolved in a policyholder's favor and other Company defenses are not successful, the Company's coverage obligations under the policies at issue would be materially increased and bounded only by the applicable per-occurrence limits and the number of asbestos bodily injury claims against the policyholders. Accordingly, although the Company has seen a moderation in the overall risk associated with these lawsuits, it remains difficult to predict the ultimate cost of these claims.

Many coverage disputes with policyholders are only resolved through settlement agreements. Because many policyholders make exaggerated demands, it is difficult to predict the outcome of settlement negotiations. Settlements involving bankrupt policyholders may include extensive releases which are favorable to the Company but which could result in settlements for larger amounts than originally anticipated. There also may

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be instances where a court may not approve a proposed settlement, which may result in additional litigation and potentially less beneficial outcomes for the Company. As in the past, the Company will continue to pursue settlement opportunities.

In addition to claims against policyholders, proceedings have been launched directly against insurers, including the Company, by individuals challenging insurers' conduct with respect to the handling of past asbestos claims and by individuals seeking damages arising from alleged asbestos-related bodily injuries. It is possible that the filing of other direct actions against insurers, including the Company, could be made in the future. It is difficult to predict the outcome of these proceedings, including whether the plaintiffs will be able to sustain these actions against insurers based on novel legal theories of liability. The Company believes it has meritorious defenses to these claims and has received favorable rulings in certain jurisdictions.

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Travelers Property Casualty Corp. (TPC), a wholly-owned subsidiary of the Company, had entered into settlement agreements, which are subject to a number of contingencies, in connection with a number of these direct action claims. For a full discussion of these settlement agreements, including subsequent appeals and court decisions that have delayed their implementation, see the Asbestos Direct Action Litigation section of note 12 of notes to the unaudited consolidated financial statements.

Because each policyholder presents different liability and coverage issues, the Company generally reviews the exposure presented by each policyholder at least annually. Among the factors which the Company may consider in the course of this review are: available insurance coverage, including the role of any umbrella or excess insurance the Company has issued to the policyholder; limits and deductibles; an analysis of the policyholder's potential liability; the jurisdictions involved; past and anticipated future claim activity and loss development on pending claims; past settlement values of similar claims; allocated claim adjustment expense; potential role of other insurance; the role, if any, of non-asbestos claims or potential non-asbestos claims in any resolution process; and applicable coverage defenses or determinations, if any, including the determination as to whether or not an asbestos claim is a products/completed operation claim subject to an aggregate limit and the available coverage, if any, for that claim.

The Company's quarterly asbestos reserve reviews include an analysis of exposure and claim payment patterns by policyholder category, as well as recent settlements, policyholder bankruptcies, judicial rulings and legislative actions. The Company also analyzes developing payment patterns among policyholders in the Home Office, Field Office and Assumed Reinsurance and Other categories as well as projected reinsurance billings and recoveries. In addition, the Company reviews its historical gross and net loss and expense paid experience, year-by-year, to assess any emerging trends, fluctuations, or characteristics suggested by the aggregate paid activity. Conventional actuarial methods are not utilized to establish asbestos reserves nor have the Company's evaluations resulted in any way of determining a meaningful average asbestos defense or indemnity payment.

Net asbestos paid losses in the first six months of 2012 were \$114 million, compared with \$110 million in the same period of 2011. Net asbestos reserves were \$2.33 billion at June 30, 2012, compared with \$2.44 billion at June 30, 2011.

The following table displays activity for asbestos losses and loss expenses and reserves:

(at and for the six months ended June 30, in millions)	2012	2011
Beginning reserves:		
Direct	\$ 2,780	\$ 2,941
Ceded	(341)	(393)
Net	2,439	2,548
Incurred losses and loss expenses:		
Direct		
Ceded		
Net		
Losses paid:		
Direct	120	133
Ceded	(6)	(23)
Net	114	110
Ending reserves:		

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Direct		<b>2,660</b>		2,808
Ceded		<b>(335)</b>		(370)
Net		<b>\$ 2,325</b>	<b>\$</b>	<b>2,438</b>

See Uncertainty Regarding Adequacy of Asbestos and Environmental Reserves.

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**ENVIRONMENTAL CLAIMS AND LITIGATION**

The Company continues to receive claims from policyholders who allege that they are liable for injury or damage arising out of their alleged disposition of toxic substances. Mostly, these claims are due to various legislative as well as regulatory efforts aimed at environmental remediation. For instance, the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), enacted in 1980 and later modified, enables private parties as well as federal and state governments to take action with respect to releases and threatened releases of hazardous substances. This federal statute permits the recovery of response costs from some liable parties and may require liable parties to undertake their own remedial action. Liability under CERCLA may be joint and several with other responsible parties.

The Company has been, and continues to be, involved in litigation involving insurance coverage issues pertaining to environmental claims. The Company believes that some court decisions have interpreted the insurance coverage to be broader than the original intent of the insurers and policyholders. These decisions often pertain to insurance policies that were issued by the Company prior to the mid-1980s. These decisions continue to be inconsistent and vary from jurisdiction to jurisdiction. Environmental claims when submitted rarely indicate the monetary amount being sought by the claimant from the policyholder, and the Company does not keep track of the monetary amount being sought in those few claims which indicate a monetary amount.

The resolution of environmental exposures by the Company generally occurs by settlement on a policyholder-by-policyholder basis as opposed to a claim-by-claim basis. Generally, the Company strives to extinguish any obligations it may have under any policy issued to the policyholder for past, present and future environmental liabilities and extinguish any pending coverage litigation dispute with the policyholder. This form of settlement is commonly referred to as a "buy-back" of policies for future environmental liability. In addition, many of the agreements have also extinguished any insurance obligation which the Company may have for other claims, including but not limited to asbestos and other cumulative injury claims. The Company and its policyholders may also agree to settlements which extinguish any liability arising from known specified sites or claims. Where appropriate, these agreements also include indemnities and hold harmless provisions to protect the Company. The Company's general purpose in executing these agreements is to reduce the Company's potential environmental exposure and eliminate the risks presented by coverage litigation with the policyholder and related costs.

In establishing environmental reserves, the Company evaluates the exposure presented by each policyholder and the anticipated cost of resolution, if any. In the course of this analysis, the Company generally considers the probable liability, available coverage, relevant judicial interpretations and historical value of similar exposures. In addition, the Company considers the many variables presented, such as: the nature of the alleged activities of the policyholder at each site; the number of sites; the total number of potentially responsible parties at each site; the nature of the alleged environmental harm and the corresponding remedy at each site; the nature of government enforcement activities at each site; the ownership and general use of each site; the overall nature of the insurance relationship between the Company and the policyholder, including the role of any umbrella or excess insurance the Company has issued to the policyholder; the involvement of other insurers; the potential for other available coverage, including the number of years of coverage; the role, if any, of non-environmental claims or potential non-environmental claims in any resolution process; and the applicable law in each jurisdiction. The evaluation of the exposure presented by a policyholder can change as information concerning that policyholder and the many variables presented is developed. Conventional actuarial techniques are not used to estimate these reserves.

In its review of environmental reserves, the Company considers: past settlement payments; changing judicial and legislative trends; its reserves for the costs of litigating environmental coverage matters; the potential for policyholders with smaller exposures to be named in new clean-up actions for both on- and off-site waste disposal activities; the potential for adverse development; the potential for additional new claims beyond previous expectations; and the potential higher costs for new settlements.





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The duration of the Company's investigation and review of these claims and the extent of time necessary to determine an appropriate estimate, if any, of the value of the claim to the Company vary significantly and are dependent upon a number of factors. These factors include, but are not limited to, the cooperation of the policyholder in providing claim information, the pace of underlying litigation or claim processes, the pace of coverage litigation between the policyholder and the Company and the willingness of the policyholder and the Company to negotiate, if appropriate, a resolution of any dispute pertaining to these claims. Because these factors vary from claim-to-claim and policyholder-by-policyholder, the Company cannot provide a meaningful average of the duration of an environmental claim. However, based upon the Company's experience in resolving these claims, the duration may vary from months to several years.

The Company continues to receive notices from policyholders tendering claims for the first time, frequently under policies issued prior to the mid-1980s. These policyholders continue to present smaller exposures, have fewer sites and are lower tier defendants. Further, in many instances, clean-up costs have been reduced because regulatory agencies are willing to accept risk-based site analyses and more efficient clean-up technologies. Over the past several years, the Company has experienced generally favorable trends in overall environmental claim payments, in the number of new policyholders tendering environmental claims for the first time and in the number of pending declaratory judgment actions relating to environmental matters. However, the degree to which those favorable trends have continued has been less than anticipated. As a result, in the second quarters of 2012 and 2011, the Company increased its net environmental reserves by \$90 million and \$76 million, respectively.

Net environmental paid losses in the first six months of 2012 and 2011 were \$44 million and \$39 million, respectively. At June 30, 2012, approximately 94% of the net environmental reserve (approximately \$365 million) was carried in a bulk reserve and included unresolved environmental claims, incurred but not reported environmental claims and the anticipated cost of coverage litigation disputes relating to these claims. The bulk reserve the Company carries is established and adjusted based upon the aggregate volume of in-process environmental claims and the Company's experience in resolving those claims. The balance, approximately 6% of the net environmental reserve (approximately \$22 million), consists of case reserves.

The following table displays activity for environmental losses and loss expenses and reserves:

(at and for the six months ended June 30, in millions)	2012	2011
Beginning reserves:		
Direct	\$ 346	\$ 354
Ceded	(5)	(3)
Net	341	351
Incurred losses and loss expenses:		
Direct	96	80
Ceded	(6)	(4)
Net	90	76
Losses paid:		
Direct	46	40
Ceded	(2)	(1)
Net	44	39
Ending reserves:		
Direct	396	394
Ceded	(9)	(6)
Net	\$ 387	\$ 388



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**UNCERTAINTY REGARDING ADEQUACY OF ASBESTOS AND ENVIRONMENTAL RESERVES**

As a result of the processes and procedures discussed above, management believes that the reserves carried for asbestos and environmental claims at June 30, 2012 are appropriately established based upon known facts, current law and management's judgment. However, the uncertainties surrounding the final resolution of these claims continue, and it is difficult to determine the ultimate exposure for asbestos and environmental claims and related litigation. As a result, these reserves are subject to revision as new information becomes available and as claims develop. The continuing uncertainties include, without limitation, the risks and lack of predictability inherent in complex litigation, any impact from the bankruptcy protection sought by various asbestos producers and other asbestos defendants, a further increase or decrease in the cost to resolve, and/or the number of, asbestos and environmental claims beyond that which is anticipated, the role of any umbrella or excess policies the Company has issued, the resolution or adjudication of disputes pertaining to the amount of available coverage for asbestos and environmental claims in a manner inconsistent with the Company's previous assessment of these claims, the number and outcome of direct actions against the Company, future developments pertaining to the Company's ability to recover reinsurance for asbestos and environmental claims and the unavailability of other insurance sources potentially available to policyholders, whether through exhaustion of policy limits or through the insolvency of other participating insurers. In addition, uncertainties arise from the insolvency or bankruptcy of policyholders and other defendants. It is also not possible to predict changes in the legal, regulatory and legislative environment and their impact on the future development of asbestos and environmental claims. This environment could be affected by changes in applicable legislation and future court and regulatory decisions and interpretations, including the outcome of legal challenges to legislative and/or judicial reforms establishing medical criteria for the pursuit of asbestos claims. It is also difficult to predict the ultimate outcome of complex coverage disputes until settlement negotiations near completion and significant legal questions are resolved or, failing settlement, until the dispute is adjudicated. This is particularly the case with policyholders in bankruptcy where negotiations often involve a large number of claimants and other parties and require court approval to be effective. As part of its continuing analysis of asbestos and environmental reserves, the Company continues to study the implications of these and other developments. (Also see note 12 of notes to the unaudited consolidated financial statements in this report).

Because of the uncertainties set forth above, additional liabilities may arise for amounts in excess of the Company's current reserves. In addition, the Company's estimate of claims and claim adjustment expenses may change. These additional liabilities or increases in estimates, or a range of either, cannot now be reasonably estimated and could result in income statement charges that could be material to the Company's operating results in future periods.

**INVESTMENT PORTFOLIO**

The Company's invested assets at June 30, 2012 were \$72.94 billion, of which 93% was invested in fixed maturity and short-term investments, 1% in equity securities, 1% in real estate and 5% in other investments. Because the primary purpose of the investment portfolio is to fund future claims payments, the Company employs a conservative investment philosophy. A significant majority of funds available for investment are deployed in a widely diversified portfolio of high quality, liquid taxable U.S. government, tax-exempt U.S. municipal and taxable corporate and U.S. agency mortgage-backed bonds.

The carrying value of the Company's fixed maturity portfolio at June 30, 2012 was \$64.71 billion. The Company closely monitors the duration of its fixed maturity investments, and investment purchases and sales are executed with the objective of having adequate funds available to satisfy the Company's insurance and debt obligations. The weighted average credit quality of the Company's fixed maturity portfolio, both including and excluding U.S. Treasury securities, was Aa2 at both June 30, 2012 and December 31, 2011. In 2011, Standard & Poor's downgraded the credit rating of securities issued by the U.S. government. The downgrade had minimal impact on the overall credit quality of the Company's fixed maturity portfolio. Below investment grade securities represented 3.1% of the total fixed maturity investment portfolio at both June 30, 2012 and December 31, 2011. The average effective duration of fixed maturities and short-term securities was 3.3 (3.5 excluding short-term securities) at June 30, 2012 and 3.2 (3.4 excluding short-term securities) at December 31, 2011.



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*Obligations of States, Municipalities and Political Subdivisions*

The Company's fixed maturity investment portfolio at June 30, 2012 and December 31, 2011 included \$38.95 billion and \$39.02 billion, respectively, of securities which are obligations of states, municipalities and political subdivisions (collectively referred to as the municipal bond portfolio). The municipal bond portfolio is diversified across the United States, the District of Columbia and Puerto Rico and includes general obligation and revenue bonds issued by states, cities, counties, school districts and similar issuers. Included in the municipal bond portfolio at June 30, 2012 and December 31, 2011 were \$8.31 billion and \$7.33 billion, respectively, of advance refunded or escrowed-to-maturity bonds (collectively referred to as pre-refunded bonds), which are bonds for which an irrevocable trust has been established to fund the remaining payments of principal and interest. Such escrow accounts are verified as to their sufficiency by an independent verification agent of the underwriter, issuer or trustee and are almost exclusively comprised of U.S. Treasury securities. Moody's Investors Service has assigned negative outlooks to municipal securities in both the state sector and local government sector within the United States.

The Company bases its investment decision on the underlying credit characteristics of the municipal security. While its municipal bond portfolio includes a number of securities that were enhanced by third-party insurance for the payment of principal and interest in the event of an issuer default, the Company does not rely on enhanced credit characteristics provided by such third-party insurance as part of its investing decisions. The downgrade during 2008 and 2009 of credit ratings of insurers of these securities resulted in a corresponding downgrade in the ratings of many such securities to the underlying rating of the respective security. Of the insured municipal securities in the Company's investment portfolio at June 30, 2012, approximately 98% were rated at A3 or above, and approximately 92% were rated at Aa3 or above, without the benefit of insurance. The Company believes that a loss of the benefit of insurance would not result in a material adverse impact on the Company's results of operations, financial position or liquidity, due to the underlying credit strength of the issuers of the securities, as well as the Company's ability and intent to hold the securities. The average credit rating of the underlying issuers of these securities was Aa2 at June 30, 2012. The average credit rating of the entire municipal bond portfolio was Aa1 at June 30, 2012 with and without the enhancement provided by third-party insurance.

*Mortgage-Backed Securities, Collateralized Mortgage Obligations and Pass-Through Securities*

The Company's fixed maturity investment portfolio at June 30, 2012 and December 31, 2011 included \$3.32 billion and \$3.52 billion, respectively, of residential mortgage-backed securities including pass-through securities and collateralized mortgage obligations (CMO), all of which are subject to prepayment risk (either shortening or lengthening of duration). While prepayment risk for securities and its effect on income cannot be fully controlled, particularly when interest rates move dramatically, the Company's investment strategy generally favors securities that reduce this risk within expected interest rate ranges. Included in the totals at June 30, 2012 and December 31, 2011 were \$1.72 billion and \$1.82 billion, respectively, of GNMA, FNMA and FHLMC (excluding FHA project loans) guaranteed residential mortgage-backed pass-through securities classified as available for sale. Also included in those totals were residential CMOs classified as available for sale with a fair value of \$1.60 billion and \$1.70 billion, at June 30, 2012 and December 31, 2011, respectively. Approximately 38% of the Company's CMO holdings were guaranteed by or fully collateralized by securities issued by GNMA, FNMA or FHLMC at both June 30, 2012 and December 31, 2011. The average credit rating of the \$996 million and \$1.05 billion of non-guaranteed CMO holdings at June 30, 2012 and December 31, 2011, respectively, was Ba2 and Ba1, respectively. The average credit rating of all of the above securities was Aa3 at both June 30, 2012 and December 31, 2011.

The Company makes investments in residential CMOs that are either guaranteed by GNMA, FNMA or FHLMC, or if not guaranteed, are senior or super-senior positions within their respective securitizations. Both guaranteed and non-guaranteed residential CMOs allocate the distribution of payments from the underlying mortgages among different classes of bondholders. In addition, non-guaranteed residential CMOs provide structures that allocate the impact of credit losses to different classes of bondholders. Senior and super-senior CMOs are protected, to varying degrees, from credit losses as those losses are initially allocated to subordinated bondholders. The Company's investment strategy is to purchase

CMO tranches that are expected to offer the most favorable return given the Company's assessment of associated risks. The Company does not purchase residual interests in CMOs.

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*Alternative Documentation Mortgages and Sub-Prime Mortgages*

At June 30, 2012 and December 31, 2011, the Company's fixed maturity investment portfolio included collateralized mortgage obligations backed by alternative documentation mortgages and asset-backed securities collateralized by sub-prime mortgages with a collective fair value of \$345 million and \$351 million, respectively (comprising approximately 0.5% of the Company's total fixed maturity investments at both dates). The continued disruption in secondary investment markets provided the Company with the opportunity to selectively acquire additional mortgage-backed securities at discounted prices in recent years. The Company purchased \$11 million and \$128 million of such securities in the six months ended June 30, 2012 and the year ended December 31, 2011, respectively. The Company defines sub-prime mortgage-backed securities as investments in which the underlying loans primarily exhibit one or more of the following characteristics: low FICO scores, above-prime interest rates, high loan-to-value ratios or high debt-to-income ratios. Alternative documentation securitizations are those in which the underlying loans primarily meet the government-sponsored entities' requirements for credit score but do not meet the government-sponsored entities' guidelines for documentation, property type, debt and loan-to-value ratios. The average credit rating on these securities and obligations held by the Company was Baa3 and Baa2 at June 30, 2012 and December 31, 2011, respectively.

*Commercial Mortgage-Backed Securities and Project Loans*

At June 30, 2012 and December 31, 2011, the Company held commercial mortgage-backed securities (including FHA project loans) of \$431 million and \$446 million, respectively.

*Equity Securities Available for Sale, Real Estate and Short-Term Investments*

See note 1 of notes to the Company's consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for further information about these invested asset classes.

*Other Investments*

At June 30, 2012 and December 31, 2011, the carrying value of the Company's other investments was \$3.47 billion and \$3.45 billion, respectively. The Company's other investments are primarily comprised of private equity limited partnerships, hedge funds, real estate partnerships, joint ventures, mortgage loans, venture capital (through direct ownership and limited partnerships) and trading securities, which are subject to more volatility than the Company's fixed maturity investments. These asset classes have historically provided a higher return than fixed maturities but are subject to more volatility. Net investment income provided by these asset classes was \$230 million and \$237 million in the six months ended June 30, 2012 and 2011, respectively.

**CATASTROPHE REINSURANCE COVERAGE**



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The Company's catastrophe reinsurance coverage is discussed in the Reinsurance section of Part I Item 1 Business in the Company's Annual Report on Form 10-K for the year ended December 31, 2011. Except as discussed below, there have been no material changes to the Company's catastrophe reinsurance coverage from that reported in the Annual Report.

*General Catastrophe Reinsurance Treaty.* The Company utilizes a general catastrophe reinsurance treaty with unaffiliated reinsurers to help manage its exposure to losses resulting from catastrophes. The general catastrophe reinsurance treaty covers the accumulation of net property losses arising out of one occurrence. The treaty covers all of the Company's exposures in the United States and Canada and their possessions and waters contiguous thereto, the Caribbean and Mexico. The treaty only provides coverage for terrorism events in limited circumstances and excludes entirely losses arising from nuclear, biological, chemical or radiological attacks.

The following table summarizes the Company's coverage under its General Catastrophe Reinsurance Treaty, effective for the period July 1, 2012 through June 30, 2013, as well as certain other catastrophe-related coverages:

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Layer of Loss	Reinsurance Coverage In-Force
\$0 - \$1.5 billion	Loss 100% retained by the Company, except for certain losses covered by the Earthquake Excess-of-Loss Treaty as described below.
\$1.5 billion - \$2.25 billion	53.3% (\$400 million) of loss covered by treaty; 46.7% (\$350 million) of loss retained by the Company. Additionally, certain losses incurred in the Northeastern United States are covered by the Catastrophe Bond Programs as described below.
Greater than \$2.25 billion	100% of loss retained by the Company, except for certain losses incurred in the Northeastern United States, which are covered by the Catastrophe Bond Programs and Northeast Catastrophe Treaty as described below.

*Catastrophe Bond Program.* With respect to Longpoint Re II, one of the Company's catastrophe bond programs, the attachment point for index-based losses and the maximum limit in the program's two reinsurance agreements are reset annually using a third-party proprietary computer model to estimate potential hurricane losses for the entire industry. Each reinsurance agreement provides up to \$250 million of coverage on a proportional basis from losses resulting from certain hurricane events in the northeastern United States. The two reinsurance agreements expire in December 2012 and 2013, respectively. The purpose of the annual reset is to maintain modeled probabilities of attachment and expected loss on the respective catastrophe bonds equal to their initial modeled probabilities. The attachment point for the indexed-based losses and maximum limit were reset in April 2012 using a new version of the third-party proprietary computer model. Accordingly, for the period May 1, 2012 through December 18, 2012, the Company will be entitled to begin recovering amounts under the two reinsurance agreements if the index-based losses in the covered area for a single occurrence reach an initial attachment amount of \$3.500 billion, up from \$2.208 billion. For the period December 19, 2012 through December 18, 2013, the Company will be able to collect up to \$250 million from the remaining reinsurance contract that expires in December 2013. The full \$250 million coverage amount of each agreement is available on a proportional basis until index-based losses reach a maximum \$4.358 billion limit, up from \$2.793 billion. Covered losses under the agreement are limited to the following geographic locations: Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island and Vermont.

On June 6, 2012, Long Point Re III Ltd. ( Long Point Re III ), a newly formed independent Cayman Islands insurance company, completed an offering of \$250 million aggregate principal amount of catastrophe bonds to investors. In connection with the offering, the Company and Long Point Re III entered into a three-year reinsurance agreement providing coverage to the Company for losses from a hurricane in the northeastern United States. Coverage under the agreement is subject to a \$2.0 billion retention, after which the Company is entitled to recover 50% of losses, up to a maximum recovery of \$250 million. The attachment point, maximum limit and insurance percentage are reset annually to maintain modeled probabilities of attachment and expected loss on the respective catastrophe bonds equal to the initial modeled probabilities of attachment and expected loss. The business covered by the reinsurance agreement comprises specified property and related coverages in the Company's Personal Insurance segment, and within the Select Accounts and the Commercial Accounts business groups within the Company's Business Insurance segment. Covered losses under the agreement are limited to the following geographic locations: Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Virginia and Vermont. Similar to Longpoint Re II, in Long Point Re III the proceeds of the offering were deposited in a reinsurance trust account. In addition, the permitted investments for such proceeds are of the same type as in Longpoint Re II in all material respects, except that in Long Point Re III the money market funds must have been rated AAAM by Standard & Poor's on the issuance date of the bonds and thereafter must only be rated by S&P. Long Point Re III was structured similarly to Longpoint Re II but does not utilize a dual trigger reinsurance agreement that is based on an index. Accordingly, the Company is not the primary beneficiary of Long Point Re III (i.e., does not consolidate that entity in the Company's consolidated financial statements) and the reinsurance agreement is accounted for as reinsurance. See the Catastrophe Reinsurance section of Part I Item 1 Business in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 for a discussion of the structure of and accounting for Longpoint Re II.



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*Other Catastrophe Reinsurance Treaties.* In addition to its general catastrophe treaty and its multi-year catastrophe bond program, the Company also is party to a northeast general catastrophe treaty, a general catastrophe aggregate excess-of-loss reinsurance treaty, an earthquake excess-of-loss reinsurance treaty and several international reinsurance treaties.

*Northeast General Catastrophe Reinsurance Treaty.* The northeast general catastrophe treaty provides up to \$600 million of coverage, subject to a \$2.25 billion retention, for losses arising from hurricanes, tornadoes, hailstorms, earthquakes and winter storm or freeze losses from Virginia to Maine for the period July 1, 2012 through June 30, 2013. Losses from a covered event (occurring over several days) anywhere in the United States, Canada, the Caribbean and Mexico and waters contiguous thereto may be used to satisfy the retention. Recoveries under the catastrophe bond programs (if any) would be first applied to reduce losses subject to this treaty.

*General Catastrophe Aggregate Excess-of-Loss Reinsurance Treaty* See Reinsurance section of Part I Item 1 Business in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

*Earthquake Excess-of-Loss Reinsurance Treaty.* The earthquake excess-of-loss treaty provides for up to \$142.5 million of coverage, subject to a \$125 million retention, for earthquake losses incurred under policies written by the National Property business unit in the Company's Business Insurance segment for the period July 1, 2012 through June 30, 2013.

The Company regularly reviews its catastrophe reinsurance coverage and may adjust such coverage in the future.

**REINSURANCE RECOVERABLES**

For a description of the Company's reinsurance recoverables, refer to Reinsurance Recoverables in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

The following table summarizes the composition of the Company's reinsurance recoverables:

(in millions)	June 30, 2012	December 31, 2011
Gross reinsurance recoverables on paid and unpaid claims and claim adjustment expenses	\$ 5,522	\$ 6,255
Allowance for uncollectible reinsurance	(270)	(345)
<b>Net reinsurance recoverables</b>	<b>5,252</b>	<b>5,910</b>
Mandatory pools and associations	1,961	2,020
Structured settlements	3,191	3,225
<b>Total reinsurance recoverables</b>	<b>\$ 10,404</b>	<b>\$ 11,155</b>

The \$658 million decline in net reinsurance recoverables since December 31, 2011 primarily reflected the impact of cash collections, including commutation agreements, and the impact of net favorable prior year reserve development in the first six months of 2012.

## OUTLOOK

The following discussion provides outlook information for certain key drivers of the Company's results of operations and capital position.

*Premiums.* The Company's earned premiums are a function of net written premium volume. Net written premiums comprise both renewal business and new business and are recognized as earned premium over the life of the underlying policies. When business renews, the amount of net written premiums associated with that business may increase or decrease (renewal premium change) as a result of increases or decreases in rate and/or insured exposures, which the Company considers as a measure of units of exposure. Net written premiums from both renewal and new business, and therefore earned premiums, are impacted by competitive market conditions as well as general economic conditions, which, particularly in the case of the Business Insurance segment, affect audit premium adjustments, policy endorsements and mid-term cancellations. Net written premiums are also impacted by the structure of reinsurance programs and related costs.

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Given the possibility that more active weather patterns such as the Company experienced in recent periods may continue, as well as the possibility that interest rates may remain low for some period of time, along with the current level of profitability in certain of its product lines, the Company is undertaking efforts to improve its underwriting margins. These efforts include seeking improved rates, as well as improved terms and conditions on many of its insurance products, and may also include other initiatives, such as reducing operating expenses and acquisition costs. These efforts may not be successful and/or may result in lower retention and new business levels and therefore lower business volumes. Nonetheless, the Company currently expects retention levels (the amount of expiring premium that renews, before the impact of renewal premium changes) will remain strong relative to historical experience. The Company also expects to continue to achieve renewal price increases during the remainder of 2012 and into 2013. In the Business Insurance segment, the Company expects that renewal premium changes during the remainder of 2012 and into 2013 will be broadly consistent with the higher levels attained in the first six months of 2012 and will be driven by increases in both renewal rate changes and, subject to the economic uncertainties discussed below, insured exposures. In the Financial, Professional & International Insurance segment, the Company expects that renewal premium changes will modestly improve during the remainder of 2012 and into 2013 compared to the first six months of 2012. In the Personal Insurance segment, the Company expects both Agency Automobile and Agency Homeowners and Other renewal premium changes during the remainder of 2012 and into 2013 will remain positive and will be slightly higher than in the first six months of 2012 based on the Company's actions to file for rate increases. The need for state regulatory approval for changes to personal property and casualty insurance prices, as well as competitive market conditions, may impact the timing and extent of renewal premium changes.

The pricing environment for new business generally has less of an impact on underwriting profitability than renewal rate changes, given the volume of new business relative to renewal business. Property and casualty insurance market conditions are expected to remain competitive during the remainder of 2012 and into 2013 for new business, not only in Business Insurance and Financial, Professional & International Insurance, but especially in Personal Insurance, where price comparison technology used by agents and brokers, sometimes referred to as comparative raters, has increased the focus on price over other competitive factors. In addition, in Personal Insurance, as in other segments, the need to keep pace with technological changes, such as telematics and other usage-based methods of determining premiums, may become an increasingly important competitive factor. In Personal Insurance, the Company's efforts to seek improved rates and terms and conditions have impacted, and are likely to continue to impact, the level of new business. See Item 1A Risk Factors The intense competition that we face could harm our ability to maintain or increase our business volumes and our profitability in the Company's Annual Report on Form 10-K for the year ended December 31, 2011. In addition, the Company launched a new distribution channel in 2009 that markets personal insurance products directly to consumers, which is expected to generate modest growth in premium volume for Personal Insurance during the remainder of 2012 and into 2013.

Current economic conditions have been somewhat volatile and there is increased uncertainty as to whether the U.S. or the global economy will grow modestly, remain stagnant or enter a recession. Economic growth experienced in 2011 and the first six months of 2012 may or may not continue, or may continue at a slower rate for an extended period of