Management's Discussion & Analysis of
Financial Condition and Results of Operations

Quarter Ended June 30, 2005

Management's Discussion & Analysis of Financial Condition and Results of Operations

The following discussion highlights significant factors influencing results of operations and changes in financial position of Liberty Mutual Holding Company Inc., the parent corporation of the Liberty Mutual Group of companies (the "Company" or "LMG"), for the three and six months ended June 30, 2005 and 2004. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's Annual Report, Second Quarter 2005 Consolidated Financial Statements, Second Quarter 2005 Financial Supplement (unaudited) and First Quarter 2005 MD&A located on the Company's Investor Relations web site at www.libertymutual.com/investors. The Company's discussions related to net income are presented on an after-tax GAAP basis. All other discussions are presented on a pre-tax GAAP basis, unless otherwise noted.

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Cautionary Statement Regarding Forward-Looking Statements

This report contains forward-looking statements that are intended to enhance the reader's ability to assess the Company's future financial and business performance. Forward-looking statements include, but are not limited to, statements that represent the Company's beliefs concerning future operations, strategies, financial results or other developments, and contain words and phrases such as "may," "expects," "should," "believes," "anticipates," "estimates," "intends" or similar expressions. Because these forward-looking statements are based on estimates and assumptions that are subject to significant business, economic and competitive uncertainties, many of which are beyond the Company's control or are subject to change, actual results could be materially different.

In particular, the sufficiency of the Company's reserves for (i) asbestos, (ii) environmental, and (iii) toxic tort (i.e., claims that arise primarily from exposure to chemical or other hazardous substances, including welding rod and silica related claims ((i), (ii), and (iii) together "A&E"), as well as its results of operations, financial condition and liquidity, to the extent impacted by the sufficiency of the Company's A&E reserves, are subject to a number of potential adverse developments including adverse developments involving A&E claims and the related level and outcome of litigation, the willingness of parties, including the Company, to settle disputes, the interpretation of aggregate policy coverage limits, the Company's ability to recover reinsurance for A&E and other claims, the legal, economic, regulatory, and legislative environments, and their impact on the future development of A&E claims, and the impact of bankruptcies of various asbestos producers and related peripheral businesses.

Some of the other factors that could cause actual results to differ include, but are not limited to, the following: the Company's inability to obtain price increases due to competition or otherwise; the performance of the Company's investment portfolios, which could be adversely impacted by adverse developments in U.S. and global financial markets, interest rates and rates of inflation; weakening U.S. and global economic conditions; insufficiency of, or changes in, loss reserves; the occurrence of catastrophic events, both natural and man-made, including terrorist acts, with a severity or frequency exceeding the Company's expectations; exposure to, and adverse developments involving, environmental claims and related litigation; the impact of claims related to exposure to potentially harmful products or substances, including, but not limited to, lead paint, silica and other potentially harmful substances; adverse changes in loss cost trends, including inflationary pressures in medical costs and auto and home repair costs; developments relating to coverage and liability for mold claims; the effects of corporate bankruptcies on surety bond claims; adverse developments in the cost, availability and/or ability to collect reinsurance; the ability of the Company's subsidiaries to pay dividends to the Company; adverse results or other consequences from legal proceedings; the impact of regulatory investigations or reforms, including governmental actions regarding the compensation of brokers and agents and the purchase and sale of nontraditional products and related disclosures; unusual loss activity resulting from adverse weather conditions, including storms, hurricanes, hail, snowfall and winter conditions; repatriation of foreign earnings; judicial expansion of policy coverage and the impact of new theories of liability; the impact of legislative actions, including Federal and state legislation related to asbestos liability reform; larger than expected assessments for guaranty funds and mandatory pooling arrangements; a downgrade in the Company's claims-paying and financial strength ratings; the loss or significant restriction on the Company's ability to use credit scoring in the pricing and underwriting of Personal Lines policies; and amendments and changes to the risk-based capital requirements. The Company's forward-looking statements speak only as of the date of this report or as of the date they are made and should be regarded solely as the Company's current plans, estimates and beliefs. For a detailed discussion of these and other cautionary statements, visit the Company's Investor Relations web site at www.libertymutual.com/investors. The Company undertakes no obligation to update these forward-looking statements.

EXECUTIVE SUMMARY

The following highlights do not address all of the matters covered in the other sections of Management's Discussion & Analysis of Financial Condition and Results of Operations or contain all of the information that may be important to the investing public. This summary should be read in conjunction with the other sections of Management's Discussion & Analysis of Financial Condition and Results of Operations and the Company's unaudited financial statements.

Three Months Ended June 30, 2005 - Consolidated Results of Operations

- Revenues for the three months ended June 30, 2005 were $5.290 billion, an increase of $509 million or 10.6% over the same period in 2004.

- Pre-tax income for the three months ended June 30, 2005 was $630 million, an increase of $237 million or 60.3% over the same period in 2004.

- Net income for the three months ended June 30, 2005 was $500 million, an increase of $93 million or 22.9% over the same period in 2004. Included in this amount is $127 million of Federal and foreign income tax expense, as the Company reduced its domestic deferred tax valuation allowance to zero in the second quarter of 2005.

- Cash flow from operations for the three months ended June 30, 2005 was $889 million, an increase of $185 million or 26.3% over the same period in 2004.

- The combined ratio before catastrophes[1], net incurred losses attributable to prior years[2] and discount accretion for the three months ended June 30, 2005 was 95.1%, a decrease of 0.7 points from the same period in 2004. Including the impact of catastrophes, net incurred losses attributable to prior years and discount accretion, the Company's combined ratio increased 0.3 points to 99.1% in 2005.

Six Months Ended June 30, 2005 - Consolidated Results of Operations

- Revenues for the six months ended June 30, 2005 were $10.261 billion, an increase of $776 million or 8.2% over the same period in 2004.

- Pre-tax income for the six months ended June 30, 2005 was $1.035 billion, an increase of $360 million or 53.3% over the same period in 2004.

- Net income for the six months ended June 30, 2005 was $896 million, an increase of $205 million or 29.7% over the same period in 2004. Included in this amount is $127 million of Federal and foreign income tax expense, as the Company reduced its domestic deferred tax valuation allowance to zero in the second quarter of 2005.

- Cash flow from operations for the six months ended June 30, 2005 was $1.747 billion, an increase of $194 million or 12.5% over the same period in 2004.

- The combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion for the six months ended June 30, 2005 was 96.0%, a decrease of 1.3 points from the same period in 2004. Including the impact of catastrophes, net incurred losses attributable to prior years and discount accretion, the Company's combined ratio decreased 1.9 points to 99.1% in 2005.

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[1] Catastrophes, net of reinstatement premium, exclude losses related to the Company's reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472 (formerly Lloyd's Syndicates 282 and 190)), except for losses related to Hurricanes Charley, Frances, Ivan and Jeanne ("four hurricanes"), which had a material impact on the Company's results.

[2] Net incurred losses attributable to prior years is defined as incurred losses attributable to prior years (excluding prior year losses related to the four hurricanes of 2004) net of earned premium attributable to prior years and amortization of retroactive reinsurance gain and excluding discount accretion.

Financial Condition as of June 30, 2005

- Total assets increased to $75.655 billion as of June 30, 2005, an increase of $3.296 billion or 4.6% over December 31, 2004.

- Policyholders' equity was $9.588 billion as of June 30, 2005, an increase of $891 million or 10.2% over December 31, 2004.

- Net unrealized gains on fixed maturities, net of tax as of June 30, 2005 were $955 million, an increase of $96 million or 11.2% over December 31, 2004.

- Statutory surplus as regards policyholders for the combined operations of Liberty Mutual Insurance Company ("LMIC") and its U.S. affiliates was $9.867 billion, an increase of $1.128 billion or 12.9% over December 31, 2004.

- The consolidated debt to capital ratio including accumulated other comprehensive income ("AOCI") as of June 30, 2005 was 21.3%, an increase of 0.2 points over December 31, 2004. Excluding AOCI, the consolidated debt to capital ratio was 23.7%, a decrease of 0.1 points from December 31, 2004.

Other 2005 2nd Quarter Highlights

Organizational Changes

- On June 22, 2005, the Company announced that Roger L. Jean, president of its Regional Agency Markets operations and an executive vice president with the Company, will retire in early 2006. In anticipation of Mr. Jean's departure and to more effectively serve third party distributors, Liberty Mutual created a new strategic business unit effective, July 5, 2005. Gary R. Gregg, formerly Liberty Mutual Group's executive vice president and manager of Commercial Markets, became president of the newly formed Agency Markets business unit, which includes the operations of Regional Agency Markets ("RAM"), Wausau Commercial Markets and Surety, formerly part of Commercial Markets. David H. Long, formerly chief operating officer of the Company's National Market business, replaced Mr. Gregg as executive vice president and manager of Commercial Markets. The Company will begin reporting its results consistent with the organizational changes in the third quarter of 2005.

Revolving Credit Facility

- Liberty Mutual Group Inc. ("LMGI") entered into a new $750 million five-year revolving credit agreement, which became effective on July 25, 2005. This agreement replaced the Company's previous credit facility ($450 million 364-day). The facility supports LMGI's $600 million commercial paper program and is available to provide working capital to the Company's domestic insurance companies. The five-year credit agreement is guaranteed by LMIC. To date, no funds have been borrowed under the facility.

Subsequent Events

Legal and Regulatory Matters

- As previously disclosed, the Company has received subpoenas and other requests for information from insurance, governmental and enforcement authorities as part of the on-going investigation of the insurance industry. In addition to the previously disclosed private civil litigation in Essex County, Massachusetts, the Company was recently named in the Insurance Brokerage Antitrust Litigation filed in the U.S. District Court of New Jersey. Both suits seek monetary and injunctive relief. The Company believes that it has substantial defenses to these pending suits and intends to defend each of the actions vigorously. As the sixth largest property and casualty insurer in the United States based on 2004 direct written premium, the Company expects that it may receive additional subpoenas or requests for information and be named in additional civil suits as the investigations continue.

  In June 2005, a non-executive, non-management employee resigned from the Company after an investigator found external evidence of improper behavior. In August 2005, this former employee pleaded guilty to a misdemeanor charge of restricting competition. The Company has cooperated with all regulatory authorities in connection with these industry investigations and will continue to do so.

CONSOLIDATED RESULTS OF OPERATIONS

The Company has identified consolidated pre-tax operating income ("PTOI") and net written premium as non-GAAP financial measures. PTOI is defined by the Company as net income excluding net realized gains (losses), Federal and foreign income taxes, extraordinary items, discontinued operations and cumulative effect of changes in accounting principles. PTOI is considered by the Company to be an appropriate indicator of underwriting and operating results and is consistent with the way the Company internally evaluates performance, except that limited partnership results recognized on the equity method are not included in internal PTOI. Net realized investment gains (losses) are significantly impacted by both discretionary and economic factors and are not necessarily indicative of operating results. Federal and foreign income taxes are significantly impacted by permanent differences and valuation allowances. References to "direct written premium" represent the amount of premium recorded for policies issued during a fiscal period, excluding assumed reinsurance and ignoring the effects of ceded reinsurance. References to "net written premium" represent the amount of premium recorded for policies issued during a fiscal period including reinsurance assumed, and audit and retrospectively rated premium related to loss sensitive policies less reinsurance ceded. In addition, the majority of workers compensation premium is adjusted to the "booked as billed" method through the Corporate & Other segment. "Premium earned," which is the portion of premium that applies to the expired part of the policy period, is a GAAP measure. The Company believes that net written premium is a performance measure useful to investors as it generally reflects current trends in the Company's sale of property and casualty insurance products.

The Company's discussions related to net income are presented on an after-tax GAAP basis. All other discussions are presented on a pre-tax GAAP basis, unless otherwise noted.

(1) Overview – Consolidated

Consolidated net written premium by significant line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Private passenger automobile	$1,435	$1,472	(2.5%)	$2,713	$2,821	(3.8%)
Workers compensation	861	826	4.2	2,103	1,990	5.7
Commercial multiple peril / Fire	363	324	12.0	700	629	11.3
Homeowners	417	390	6.9	743	696	6.8
Commercial automobile	273	239	14.2	562	530	6.0
LIU[1] reinsurance	198	218	(9.2)	469	508	(7.7)
International local businesses [2]	231	189	22.2	484	403	20.1
General liability	176	309	(43.0)	363	509	(28.7)
LIU[1] third party	113	92	22.8	207	173	19.7
Group disability	87	86	1.2	172	168	2.4
LIU[1] first party	52	68	(23.5)	126	158	(20.3)
Surety	52	33	57.6	100	66	51.5
Assumed voluntary reinsurance	21	30	(30.0)	48	66	(27.3)
Other	143	143	-	289	272	6.3
Total net written premium	$4,422	$4,419	0.1%	$9,079	$8,989	1.0%

1 Liberty International Underwriters (LIU)
2 Small commercial and other personal; excludes private passenger automobile.

Consolidated net written premium by strategic business unit was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Personal Market	$1,363	$1,426	(4.4%)	$2,524	$2,672	(5.5%)
Commercial Markets	1,045	1,148	(9.0)	2,507	2,600	(3.6)
Regional Agency Markets	1,118	1,024	9.2	2,200	2,003	9.8
International	923	837	10.3	1,934	1,786	8.3
Corporate and Other	(27)	(16)	68.8	(86)	(72)	19.4
Total net written premium	$4,422	$4,419	0.1%	$9,079	$8,989	1.0%

Net written premium for the three and six months ended June 30, 2005 was $4.422 billion and $9.079 billion, respectively, representing increases of $3 million and $90 million over the same periods in 2004. Both periods reflect strong premium growth in RAM (primarily due to Summit Holdings Southeast Inc. and affiliates ("Summit"), a mono-line workers compensation business with operations primarily in Florida) and International (due to the local businesses). Partially offsetting these increases were decreases in premium related to the Company's private passenger automobile business in both Personal Market and RAM and the loss of a large general liability account in Commercial Markets.

Significant changes by major line of business include:

- Workers compensation net written premium increased $35 million and $113 million in the quarter and year-to-date, respectively, primarily due to exposure growth in Summit.
- Commercial multiple peril / fire net written premium increased $39 million and $71 million in the quarter and year-to-date, respectively, primarily due to improved retention in RAM.
- Homeowners net written premium increased $27 million and $47 million, in the quarter and year-to-date, respectively, primarily due to rate increases and new business growth in the Company's Personal Market.
- General liability net written premium decreased $133 million and $146 million in the quarter and year-to-date, respectively, primarily driven by the loss of a large National Market account due to more aggressive price competition.
- Private passenger automobile net written premium decreased $37 million and $108 million in the quarter and year-to-date, respectively, primarily due to the conversion of PruPac[1] six-month term policies to twelve-month term policies during 2004, lower retention on the PruPac business and lower average premium per policy related to a reduction in higher premium involuntary market policies, a shift in state mix and a general improvement in the quality of the risk underwritten. Also contributing to the decrease in both periods was the Company's re-underwriting efforts, expanded rating tiers and active non-renewal of certain classes of business in RAM. Partially offsetting these decreases was growth in International's local business operations, rate increases and an increase in policies in force in Personal Market's non-PruPac business, driven by new business growth.

More detailed explanations of the changes in net written premium by line of business are included in the related discussion of financial results for each strategic business unit.

For a fuller description of the Company's business operations, products and distribution channels, please visit the Company's Investor Relations web site at www.libertymutual.com/investors.

[1] The Company acquired Prudential Financial Inc.'s U.S. personal lines property and casualty business ("PruPac") in the fourth quarter of 2003.

Results of Operations – Consolidated

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Revenues	$5,290	$4,781	10.6%	$10,261	$9,485	8.2%
PTOI before catastrophes, net incurred losses attributable to prior years and discount accretion	$609	$471	29.3%	$1,085	$863	25.7%
Catastrophes[1]:						
- Four hurricanes 2004	(39)	-	NM	(44)	-	NM
- All other	(46)	(55)	(16.4)	(80)	(96)	(16.7)
Net incurred losses attributable to prior years:						
- Asbestos	(2)	(4)	(50.0)	(2)	(4)	(50.0)
- All other[2]	(54)	(32)	68.8	(83)	(134)	(38.1)
Discount accretion[3]	(23)	(24)	(4.2)	(47)	(48)	(2.1)
Pre-tax operating income	445	356	25.0	829	581	42.7
Realized investment gains, net	185	37	NM	206	94	119.1
Federal and foreign income tax expense	(127)	-	NM	(127)	-	NM
Discontinued operations, net of tax	(3)	14	NM	(12)	16	NM
Extraordinary items, net of tax	-	-	-	-	-	-
Net income	$500	$407	22.9%	$896	$691	29.7%

1 The Company does not typically identify catastrophe losses from assumed reinsurance lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) in the tables above given the expected volatility associated with property-reinsurance coverage. However, due to the significant impact that the four hurricanes had on the Company's results, these losses have been separately identified in the tables above. Catastrophe losses include the impact of reinstatement premiums.

2 Net of earned premium attributable to prior years of $0 and $8 million for the three and six months ended June 30, 2005, respectively, and $38 million and $58 million for the comparable periods of 2004. Net of amortization of deferred gains on retroactive reinsurance of $46 million and $58 million for the three and six months ended June 30, 2005, respectively, and $12 million and $23 million for the comparable periods of 2004.

3 The Company discounts the long-term indemnity portion of its workers compensation claims as permitted by insurance regulations. The discount accretion on these claims is included in underwriting results as the loss reserves accrete to nominal value. Asbestos structured settlements are discounted at 4.5%.

NM = Not Meaningful (represents increases or decreases greater than 200%, or changes from a net gain to a net loss, or vice versa).

Revenues for the three and six months ended June 30, 2005 were $5.290 billion and $10.261 billion, respectively, representing increases of $509 million and $776 million over the same periods in 2004. The major components of revenues include net premium earned, net investment income, net realized investment gains/losses and fee and other revenues.

Net premium earned for the three and six months ended June 30, 2005 was $4.332 billion and $8.537 billion, respectively, representing increases of $263 million and $501 million over the same periods in 2004. The increases in both periods reflect modest rate increases, new business growth and improved customer retention across many of the Company's major segments. Net earned premium attributable to prior years was $38 million and $50 million less for the three and six months ended June 30, 2005, respectively, versus the prior periods.

Net investment income for the three and six months ended June 30, 2005 was $593 million and $1.148 billion, respectively, representing increases of $73 million and $126 million over the same periods in 2004. The improvement reflects an increase of $21 million and $60 million in interest income in the quarter and year-to-date, respectively, primarily due to a higher invested asset base as the Company continues to generate significant cash flow from operations. In addition, the Company reported increases of $42 million and $65 million in the quarter and year-to-date, respectively, from limited partnership income related to private equity investments.

Net realized investment gains for the three and six months ended June 30, 2005 were $185 million and $206 million, respectively, representing increases of $148 million and $112 million over the same periods in 2004. The improvement in the quarter reflects increases of $71 million in other investments primarily related to energy gains, $66 million in equities driven by gains on sales of foreign equities and private equity investments, and $11 million in fixed maturities. The improvement year-to-date reflects higher gains in equities and other investments of $54 million and $76 million, respectively, partially offset by a decrease in fixed maturities of $18 million. In addition, impairment losses decreased $8 million and $21 million in the quarter and year-to-date, respectively, from the comparable periods in 2004.

Fee and other revenues for the three and six months ended June 30, 2005 were $180 million and $370 million, respectively, representing increases of $25 million and $37 million over the same periods in 2004. The improvement primarily reflects increases in fee and other revenues from the production and sale of oil and gas from Liberty Energy Holdings, LLC ("Liberty Energy") and the Company's involuntary market servicing carrier operations.

Claims, benefits and expenses for the three and six months ended June 30, 2005 were $4.660 billion and $9.226 billion, respectively, representing increases of $272 million and $416 million over the same periods in 2004. The increase in both periods reflects business growth and general cost increases, including higher personnel costs, interest expense and variable compensation expense. In addition, catastrophe losses related to the four hurricanes of 2004 increased in both periods, primarily due to delayed reporting of losses in International's reinsurance business in the quarter. Also contributing to the increase in both periods was higher profit sharing and amortization of deferred acquisition costs attributable to the PruPac business acquired in 2003. Upon acquisition, the PruPac deferred policy acquisition costs were written off against the negative goodwill, in accordance with GAAP accounting, which resulted in less amortization of deferred acquisition cost in 2004 as compared to 2005. Partially offsetting these increases in both periods was a general improvement in current year underwriting results and a decrease in incurred losses attributable to prior years[1] of $19 million and $104 million for the three and six months ended June 30, 2005, respectively, which includes increases of $34 million and $35 million, respectively, for amortization of deferred gains on retroactive reinsurance based on the Company's re-estimation of the deferred gains and associated amortization in the second quarter of 2005. The decrease in year-to-date incurred losses attributable to prior years primarily reflects lower losses related to workers' compensation, the non-recurrence of prior year development on LIU's business in the first quarter of 2004, and the reapportionment of involuntary market liabilities, partially offset by an increase in prior year incurred losses related to RAM's commercial multiple peril and auto liability lines.

[1] Incurred losses attributable to prior years is defined as net incurred losses attributable to prior years (excluding prior year losses related to the four hurricanes of 2004) gross of earned premium attributable to prior years and including discount accretion and amortization of retroactive reinsurance gain.

CONSOLIDATED	Three Months Ended June 30, 2005	2004	Change (Points)	Six Months Ended June 30, 2005	2004	Change (Points)
Combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion						
Claims and claim adjustment expense ratio	67.3%	70.2%	(2.9)	68.4%	71.6%	(3.2)
Underwriting expense ratio	27.9	25.3	2.6	27.6	25.4	2.2
Dividend ratio	(0.1)	0.3	(0.4)	-	0.3	(0.3)
Subtotal	95.1	95.8	(0.7)	96.0	97.3	(1.3)
Catastrophes[1]:						
- Four hurricanes 2004	1.0	-	1.0	0.5	-	0.5
- All other	1.1	1.4	(0.3)	1.0	1.3	(0.3)
Net incurred losses attributable to prior years:						
- Asbestos	-	0.1	(0.1)	-	0.1	(0.1)
- All other	1.3	0.9	0.4	1.0	1.7	(0.7)
Discount accretion	0.6	0.6	-	0.6	0.6	-
Total combined ratio[2]	99.1%	98.8%	0.3	99.1%	101.0%	(1.9)

[1] The Company does not typically identify catastrophe losses from assumed reinsurance lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) in the tables above given the expected volatility associated with property-reinsurance coverage. However, due to the significant impact that the four hurricanes had on the Company's results, these losses have been separately identified in the tables above. Catastrophe losses include the impact of reinstatement premiums.

[2] The combined claim and expense ratio, expressed as a percentage, is a measure of underwriting profitability. This measure should only be used in conjunction with, and not in lieu of, underwriting income and may not be comparable to other performance measures used by the Company's competitors. The combined claim and expense ratio is computed as the sum of the following property and casualty ratios: the ratio of claims and claim adjustment expense to earned premium; the ratio to earned premium of insurance operating costs plus amortization of deferred policy acquisition costs less fee income (primarily related to the Company's involuntary market servicing carrier operations) and less installment charges; and the ratio of policyholder dividends to earned premium. Provisions for uncollectible premium and reinsurance are not included in the combined ratio. Beginning in the second quarter of 2004, results of the Company's Group Market operations have been excluded from the above table and related discussion of the combined ratio. Prior periods have been restated to conform to the current presentation.

The consolidated combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion for the three and six months ended June 30, 2005 was 95.1% and 96.0%, respectively, representing decreases of 0.7 and 1.3 points over the comparable periods in 2004. Results in both periods reflect the favorable impact of underwriting and pricing actions taken and a lower dividend ratio, partially offset by a higher underwriting expense ratio. The lower dividend ratio in both periods was due to the Company's re-evaluation of its estimate of dividend reserves in the second quarter which resulted in a reduction of the required liability. In addition, the year-to-date dividend ratio was favorably impacted by the recoupment of a previously paid dividend during the first quarter of 2005. The higher expense ratio in both periods reflects increases in variable incentive compensation, personnel costs, profit sharing and amortization of deferred policy acquisition costs related to the PruPac acquisition and other general expenses. Including the impact of catastrophes, net incurred losses attributable to prior years and discount accretion, the total combined ratio was 99.1% for the quarter and year-to-date, representing a 0.3 point increase and 1.9 point decrease, respectively, versus the same periods in 2004. The combined ratio increase for the quarter reflects 1.0 point of additional losses associated with the four hurricanes of 2004, primarily a result of late reporting to LIU. Additionally, the combined ratio in the quarter reflects a 0.3 point increase in net incurred losses attributable to prior years related to lower prior year premium recognized in 2005 versus 2004, partially offset by a decrease in incurred losses related to higher amortization of deferred gains on retroactive reinsurance. The year-to-date combined ratio reflects a 0.8 point decrease in net incurred losses attributable to prior years primarily due to lower losses related to workers' compensation, the non-recurrence of prior year development on LIU's business, the

reapportionment of involuntary market liabilities, and higher amortization of deferred gains on retroactive reinsurance.

PTOI for the three and six months ended June 30, 2005 was $445 million and $829 million, respectively, representing increases of $89 million and $248 million over the same periods in 2004.

Federal and foreign income tax expense for the three and six months ended June 30, 2005 of $127 million, representing increases of $127 million over the same periods in 2004. The Company's effective tax rates for the three and six months ended June 30, 2005 were 20% and 12%, respectively, compared to 0% in the same periods of 2004. The increase in the Company's effective tax rate in both periods reflects the reduction in the domestic tax valuation allowance to zero in the second quarter of 2005. Included in the second quarter 2005 income tax expense is a $22 million tax charge incurred for planned repatriation of profits pursuant to the American Jobs Creation Act of 2004, and $15 million of tax expense for prior year taxes resulting from a judicial decision in Brazil.

Net income for the three and six months ended June 30, 2005 was $500 million and $896 million, respectively, representing increases of $93 million and $205 million over the same periods in 2004. Results from discontinued operations in 2005 reflect a loss on the disposal of certain pension business in Spain, which was a part of the acquisition of Genesis Seguros Generales, S.A. and its subsidiary Seguros Genesis S.A. (collectively, "Genesis"). Results from discontinued operations in 2004 primarily reflect a gain on the Company's Canadian personal lines business, which was sold to Meloche Monnex Inc., a member of TD Bank Financial Group ("Meloche Monnex"), on April 1, 2004.

PERSONAL MARKET

(1) Overview – Personal Market

Personal Market net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Private passenger automobile	$983	$1,071	(8.2%)	$1,848	$2,037	(9.3%)
Homeowners and other	380	355	7.0	676	635	6.5
Total net written premium	$1,363	$1,426	(4.4%)	$2,524	$2,672	(5.5%)

Net written premium for the three and six months ended June 30, 2005 was $1.363 billion and $2.524 billion, respectively, representing decreases of $63 million and $148 million from the same periods in 2004. The decrease in net written premium in both periods is a result of the conversion of PruPac six-month term auto policies to twelve-month term policies during 2004, lower retention on the PruPac auto and homeowners business and lower average written premium per auto policy, partially offset by rate increases and an increase in policies in force in the non-PruPac business, driven by new business growth.

Private passenger automobile net written premium for the three and six months ended June 30, 2005 was $983 million and $1.848 billion, respectively, representing decreases of $88 million and $189 million from the same periods in 2004. The decrease in both periods is related to the aforementioned PruPac policy conversion, lower retention on the PruPac business and lower average written premium per policy, partially offset by rate increases and an increase in policies in force in the non-PruPac business, driven by new business growth. The lower average written premium per policy reflects a reduction in higher premium involuntary market policies, a shift in state mix and a general improvement in the quality of the risks underwritten, partially offset by rate increases.

Homeowners and other net written premium for the three and six months ended June 30, 2005 was $380 million and $676 million, respectively, representing increases of $25 million and $41 million over the same periods in 2004. The increase in both periods is primarily due to rate increases and an increase in policies in force in the non-PruPac business, driven by new business growth, partially offset by lower retention on the PruPac business.

(2) *Results of Operations – Personal Market*

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Revenues	$1,354	$1,321	2.5%	$2,695	$2,640	2.1%
PTOI before catastrophes, net incurred losses attributable to prior years and discount accretion	$214	$222	(3.6%)	$403	$340	18.5%
Catastrophes:						
- Four hurricanes 2004	-	-	-	-	-	-
- All other	(34)	(32)	6.3	(61)	(62)	(1.6)
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other[1]	-	-	-	7	-	NM
Discount accretion	-	-	-	-	-	-
Pre-tax operating income[2]	180	190	(5.3)	349	278	25.5
Realized investment gains, net	-	-	-	-	-	-
Federal and foreign income tax expense	(63)	(66)	(4.5)	(122)	(97)	25.8
Discontinued operations, net of tax	-	14	NM	-	15	NM
Extraordinary items, net of tax	-	-	-	-	-	-
Net income	$117	$138	(15.2%)	$227	$196	15.8%

1 Net of earned premium attributable to prior years of $1 million and ($4) million for the three and six months ended June 30, 2005, respectively.

2 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

NM = Not meaningful

Revenues for the three and six months ended June 30, 2005 were $1.354 billion and $2.695 billion, respectively, representing increases of $33 million and $55 million over the same periods in 2004. The major components of revenues include net premium earned and net investment income.

Net premium earned for the three and six months ended June 30, 2005 was $1.279 billion and $2.536 billion, respectively, representing increases of $45 million and $68 million over the same periods in 2004. The increase in both periods is primarily due to rate increases and new business growth, partially offset by lower retention levels, primarily related to the PruPac business.

Net investment income for the three and six months ended June 30, 2005 was $62 million and $131 million, respectively, representing decreases of $11 million and $13 million from the same periods in 2004. The decrease in both periods is primarily due to lower investment yields partially offset by continued positive cash flow from operations.

Claims, benefits and expenses for the three and six months ended June 30, 2005 were $1.174 billion and $2.346 billion, respectively, a $43 million increase and $16 million decrease versus the same periods in 2004. The increase in the quarter reflects higher profit sharing and amortization of deferred acquisition costs attributable to the PruPac business acquired in 2003 along with higher personnel costs and other expenses, partially offset by favorable loss trends. Upon acquisition, the PruPac deferred policy acquisition costs were written off against the negative goodwill, in accordance with GAAP accounting, which resulted in less amortization of deferred acquisition cost in 2004 as compared to 2005. The decrease on a year-to-date basis reflects favorable loss trends in the auto and homeowners lines of business and negative incurred losses attributable to prior years related to business assumed from involuntary pools, partially offset by the aforementioned acquisition and general expenses.

PERSONAL MARKET	Three Months Ended June 30, 2005	2004	Change (Points)	Six Months Ended June 30, 2005	2004	Change (Points)
Combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion						
Claims and claim adjustment expense ratio[1]	64.2%	66.9%	(2.7)	66.3%	71.3%	(5.0)
Underwriting expense ratio[1]	24.3	20.5	3.8	23.1	20.4	2.7
Dividend ratio	-	-	-	-	-	-
Subtotal	88.5	87.4	1.1	89.4	91.7	(2.3)
Catastrophes:						
- Four hurricanes 2004	-	-	-	-	-	-
- All other	2.7	2.6	0.1	2.4	2.5	(0.1)
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other	-	-	-	(0.3)	-	(0.3)
Discount accretion	-	-	-	-	-	-
Total combined ratio[2]	91.2%	90.0%	1.2	91.5%	94.2%	(2.7)

1 Personal Market reclassified certain integration expenses in 2004 related to the PruPac acquisition between the claims and claim adjustment expense ratio and the underwriting expense ratio. The impact was a 0.5 and 0.6 point reclassification from the underwriting expense ratio to the claims and claims adjustment expense ratio for the quarter and year-to-date, respectively.

2 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

Personal Market's combined ratio for the three and six months ended June 30, 2005 was 91.2% and 91.5%, respectively, representing a 1.2 point increase and 2.7 point decrease versus the same periods in 2004. The increase in the quarter reflects an increase in the expense ratio related to higher profit sharing, amortization of deferred policy acquisition costs, personnel costs and other general expenses, partially offset by favorable loss trends in the auto and homeowners lines of business. The year-to-date decrease reflects favorable loss trends and a 0.3 point decrease in net incurred losses attributable to prior years relating to business assumed from involuntary pools, partially offset by an increase in the aforementioned acquisition and other expenses. The combined ratio before catastrophes and net incurred losses attributable to prior years was 88.5% and 89.4% in the quarter and year-to-date, respectively, representing a 1.1 point increase and 2.3 point decrease versus the comparable periods in 2004.

PTOI for the three and six months ended June 30, 2005 was $180 million and $349 million, respectively, representing a $10 million decrease and $71 million increase over the same periods in 2004.

Federal and foreign income tax expense for the three and six months ended June 30, 2005 was $63 million and $122 million, respectively, representing a $3 million decrease and $25 million increase over the same periods in 2004.

Net income for the three and six months ended June 30, 2005 was $117 million and $227 million, respectively, representing a $21 million decrease and $31 million increase over the same periods in 2004. Results from discontinued operations in 2004 primarily reflect the Company's Canadian personal lines business, which was sold to Meloche Monnex on April 1, 2004.

COMMERCIAL MARKETS

(1) Overview – Commercial Markets

Commercial Markets net written premium by market segment was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Business Market	$314	$285	10.2%	$796	$753	5.7%
National Market	281	461	(39.0)	654	829	(21.1)
Wausau Commercial Market	181	153	18.3	539	492	9.6
Specialty Risks	123	91	35.2	218	167	30.5
Group Market	87	86	1.2	172	168	2.4
Other Markets	59	72	(18.1)	128	191	(33.0)
Total net written premium	$1,045	$1,148	(9.0%)	$2,507	$2,600	(3.6%)

Commercial Markets net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Workers compensation	$540	$551	(2.0%)	$1,474	$1,456	1.2%
Commercial automobile	121	98	23.5	268	261	2.7
General liability	115	252	(54.4)	250	400	(37.5)
Group disability / life	87	86	1.2	172	168	2.4
Commercial multiple peril / Fire	71	61	16.4	128	122	4.9
Surety	52	33	57.6	100	66	51.5
Assumed voluntary reinsurance	21	30	(30.0)	48	66	(27.3)
Other	38	37	2.7	67	61	9.8
Total net written premium	$1,045	$1,148	(9.0%)	$2,507	$2,600	(3.6%)

Net written premium for the three and six months ended June 30, 2005 was $1.045 billion and $2.507 billion, respectively, representing decreases of $103 million and $93 million from the same periods in 2004. The decrease in both periods was primarily driven by the loss of a large National Market account due to more aggressive price competition. The loss of this large account coupled with lower retention were the primary reasons for the decline in general liability net written premium for both periods. Also impacting the quarter was a slight decrease in workers compensation net written premium resulting from lower audit and retrospectively rated policy premium on National Market accounts, partially offset by growth in the Business Market and Wausau Commercial Market segments. Net written premiums in the Company's Other Markets segment, which includes assumed voluntary reinsurance business, also declined in the both periods primarily due to more selective underwriting of that business in a competitive environment and a decrease in assumed involuntary net written premium in the first quarter of 2005. Partially offsetting these decreases in both periods was an increase in Specialty Risks surety premium due to a combination of increased work program utilization by existing customers and targeted new business growth in several new office locations.

(2) Results of Operations – Commercial Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Revenues	$1,391	$1,381	0.7%	$2,790	$2,708	3.0%
PTOI before catastrophes, net incurred losses attributable to prior years and discount accretion	$140	$93	50.5%	$254	$187	35.8%
Catastrophes[1]:						
- Four hurricanes 2004	(3)	-	NM	(8)	-	NM
- All other	(3)	(6)	(50.0)	(3)	(8)	(62.5)
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other[2]	(15)	(13)	15.4	(8)	(25)	(68.0)
Discount accretion[3]	(21)	(21)	-	(42)	(42)	-
Pre-tax operating income[4]	98	53	84.9	193	112	72.3
Realized investment gains, net	-	-	-	-	-	-
Federal and foreign income tax expense	(34)	(18)	88.9	(67)	(39)	71.8
Discontinued operations, net of tax	-	-	-	-	-	-
Extraordinary items, net of tax	-	-	-	-	-	-
Net income	$64	$35	82.9%	$126	$73	72.6%

1 The Company does not typically identify catastrophe losses from assumed voluntary reinsurance lines in the tables above given the expected volatility associated with property-reinsurance coverage. However, due to the significant impact that the four hurricanes had on the Company's results, these losses have been separately identified in the tables above. Catastrophe losses include the impact of reinstatement premiums.

2 Net of earned premium attributable to prior years of $(15) million and $(6) million for the three and six months ended June 30, 2005, respectively, and $30 million and $45 million for the comparable periods of 2004. Net of amortization of deferred gains on retroactive reinsurance of $31 million and $38 million for the three and six months ended June 30, 2005, respectively, and $7 million and $14 million for the comparable periods of 2004.

3 The Company discounts the long-term indemnity portion of its workers compensation claims as permitted by insurance regulations. The discount accretion on these claims is included in underwriting results as the loss reserves accrete to nominal value.

4 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

NM= Not meaningful

Revenues for the three and six months ended June 30, 2005 were $1.391 billion and $2.790 billion, respectively, representing increases of $10 million and $82 million over the same periods in 2004. The major components of revenues include net premium earned, net investment income and fee and other revenues.

Net premium earned for the three and six months ended June 30, 2005 was $1.123 billion and $2.245 billion, respectively, representing increases of $7 million and $79 million over the same periods in 2004. The increases reflect the earned premium recognition of cumulative rate increases, new business growth and improved customer retention levels over the last twelve months. These increases were partially offset by a decrease in net earned premium attributable to prior years of $45 million and $51 million for the quarter and year-to-date, respectively.

Net investment income for the three and six months ended June 30, 2005 was $172 million and $341 million, respectively, representing decreases of $2 million and $5 million from the same periods in 2004. The decrease reflects lower investment yields partially offset by a higher investment asset base and continued positive cash flow from operations.

Fee and other revenues for the three and six months ended June 30, 2005 were $96 million and $204 million, respectively, representing increases of $5 million and $8 million over the same periods in 2004. The increase was primarily due to higher fee revenues from involuntary market servicing carrier operations.

Claims, benefits and expenses for the three and six months ended June 30, 2005 were $1.293 billion and $2.597 billion, respectively, representing a $35 million decrease and $1 million increase versus the same periods in 2004. Both periods reflect a general improvement in current year underwriting results and a decrease in incurred losses attributable to prior years of $43 million and $68 million for the three and six months ended June 30, 2005, respectively. The decrease in incurred losses attributable to prior years in both periods reflects approximately $20 million of lower prior year losses in 2005 related to the reapportionment of involuntary market liabilities and approximately $24 million of higher amortization of deferred gains on retroactive reinsurance based on the Company's re-estimation of the contracts in the second quarter of 2005. The decrease year-to-date also reflects a large subrogation recovery on surety business recorded in the first quarter of 2005. These favorable decreases in the quarter and year-to-date were mostly offset by growth in the overall business and general cost increases.

	Three Months Ended June 30,			**Six Months Ended June 30,**		
COMMERCIAL MARKETS	**2005**	**2004**	**Change (Points)**	**2005**	**2004**	**Change (Points)**
Combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion						
Claims and claim adjustment expense ratio	76.8%	79.7%	(2.9)	77.4%	80.2%	(2.8)
Underwriting expense ratio	22.4	21.8	0.6	22.5	22.3	0.2
Dividend ratio	(1.3)	0.1	(1.4)	(0.7)	0.3	(1.0)
Subtotal	97.9	101.6	(3.7)	99.2	102.8	(3.6)
Catastrophes[1]:						
- Four hurricanes 2004	0.3	-	0.3	0.4	-	0.4
- All other	0.2	0.6	(0.4)	0.1	0.4	(0.3)
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other	1.5	1.3	0.2	0.4	1.1	(0.7)
Discount accretion	2.0	2.1	(0.1)	2.0	2.2	(0.2)
Total combined ratio[2]	101.9%	105.6%	(3.7)	102.1%	106.5%	(4.4)

1 The Company does not typically identify catastrophe losses from assumed voluntary reinsurance lines in the tables above given the expected volatility associated with property-reinsurance coverage. However, due to the significant impact that the four hurricanes had on the Company's results, these losses have been separately identified in the tables above. Catastrophe losses include the impact of reinstatement premiums.

2 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

The Commercial Markets combined ratio for the three and six months ended June 30, 2005 was 101.9% and 102.1%, respectively, representing decreases of 3.7 and 4.4 points from the same periods in 2004. The decrease in both periods reflects the favorable impact of underwriting and pricing actions taken and a lower dividend ratio, partially offset by a slightly higher underwriting expense ratio. The lower dividend ratio in both periods reflects the Company's re-evaluation of its estimate of dividend reserves in the second quarter which resulted in a reduction of the required liability. In addition, the year-to-date dividend ratio was favorably impacted by the recoupment of a previously paid dividend during the first quarter of 2005. Also impacting the quarter was a 0.2 point increase in net incurred losses attributable to prior years, net of premium attributable to prior years. Conversely, on a year-to-date basis, net incurred losses attributable to prior years, net of premium attributable to prior years, decreased 0.7 points. The combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion was 97.9% and 99.2% in

the quarter and year-to-date, respectively, representing decreases of 3.7 and 3.6 points from the comparable periods in 2004.

PTOI for the three and six months ended June 30, 2005 was $98 million and $193 million, respectively, representing increases of $45 million and $81 million over the same periods in 2004.

Federal and foreign income tax expense for the three and six months ended June 30, 2005 was $34 million and $67 million, respectively, representing increases of $16 million and $28 million over the same periods in 2004.

Net income for the three and six months ended June 30, 2005 was $64 million and $126 million, respectively, representing increases of $29 million and $53 million over the same periods in 2004.

REGIONAL AGENCY MARKETS (RAM)

(1) Overview – RAM

RAM net written premium by market segment was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Standard Regional Companies	$853	$816	4.5%	$1,649	$1,568	5.2%
Specialty Operations[1]	265	208	27.4	551	435	26.7
Total net written premium	$1,118	$1,024	9.2%	$2,200	$2,003	9.8%

1 Primarily includes Summit Holdings Southeast and affiliates ("Summit").

RAM net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Commercial Lines						
Workers compensation total	$402	$339	18.6%	$828	$697	18.8%
- Summit	251	195	28.7	522	410	27.3
- All other	151	144	4.9	306	287	6.6
Commercial multiple peril	272	249	9.2	531	481	10.4
Commercial automobile	152	141	7.8	294	269	9.3
General liability	41	40	2.5	78	77	1.3
Other	43	38	13.2	81	72	12.5
Subtotal	$910	$807	12.8%	$1,812	$1,596	13.5%
Personal Lines						
Private passenger automobile	$128	$138	(7.2%)	$242	$266	(9.0%)
Homeowners	72	71	1.4	130	127	2.4
Other	8	8	-	16	14	14.3
Subtotal	$208	$217	(4.1%)	$388	$407	(4.7%)
Total net written premium	$1,118	$1,024	9.2%	$2,200	$2,003	9.8%

Net written premium for the three and six months ended June 30, 2005 was $1.118 billion and $2.2 billion, respectively, representing increases of $94 million and $197 million over the same periods in 2004. Approximately $56 million and $112 million of the increase in the quarter and year-to-date, respectively, was due to Summit, a mono-line workers compensation business with operations primarily in Florida. Summit's results in both periods reflect an increase in exposure on existing accounts, partially offset by slightly lower retention and the impact of state mandated rate decreases related to Florida regulatory reform introduced in 2003. The balance of the increase in both periods reflects improved retention levels and slight rate increases across most lines. Partially offsetting the increases in both periods was a decrease in private passenger automobile net written premium due to the Company's re-underwriting efforts, expanded rating tiers and active non-renewal of certain classes of business.

(2) Results of Operations – RAM

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Revenues	$1,086	$956	13.6%	$2,131	$1,864	14.3%
PTOI before catastrophes, net incurred losses attributable to prior years and discount accretion	$121	$70	72.9%	$232	$153	51.6%
Catastrophes:						
- Four hurricanes 2004	-	-	-	-	-	-
- All other	(9)	(17)	(47.1)	(16)	(26)	(38.5)
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other[1]	(7)	9	NM	(6)	9	NM
Discount accretion	-	-	-	-	-	-
Pre-tax operating income[2]	105	62	69.4	210	136	54.4
Realized investment gains, net	3	-	NM	3	(2)	NM
Federal and foreign income tax expense	(38)	(22)	72.7	(75)	(47)	59.6
Discontinued operations, net of tax	-	-	-	-	-	-
Extraordinary items, net of tax	-	-	-	-	-	-
Net income	$70	$40	75.0%	$138	$87	58.6%

1 Net of earned premium attributable to prior years of $12 million and $13 million for the three and six months ended June 30, 2005, respectively, and $5 million and $7 million for the comparable periods of 2004.

2 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2005 were $1.086 billion and $2.131 billion, respectively, representing increases of $130 million and $267 million over the same periods in 2004. The major components of revenues include net premium earned and net investment income.

Net premium earned for the three and six months ended June 30, 2005 was $995 million and $1.954 billion, respectively, representing increases of $118 million and $244 million over the same periods in 2004. Approximately $43 million and $81 million of the increase in the quarter and year-to-date, respectively, was due to Summit, consistent with the change in its net written premium. The balance of the increase in both periods primarily reflects historical new business growth, slight rate increases and improved retention levels across most lines, partially offset by a decrease in private passenger automobile business due to the Company's re-underwriting efforts, expanded rating tiers and non-renewal of certain classes of business.

Net investment income for the three and six months ended June 30, 2005 was $72 million and $142 million, respectively, representing increases of $6 million and $12 million over the same periods in 2004. The increase reflects a higher invested asset base and continued positive cash flow from operations, partially offset by lower investment yields.

Claims, benefits and expenses for the three and six months ended June 30, 2005 were $978 million and $1.918 billion, respectively, representing increases of $84 million and $188 million over the same periods in 2004. The increase is primarily due to business growth, general cost increases and an increase in incurred losses attributable to prior years related to commercial multiple peril and auto liability lines. The increases in both periods were partially offset by lower catastrophe losses in 2005 due to favorable weather across most regions.

REGIONAL AGENCY MARKETS	Three Months Ended June 30, 2005	2004	Change (Points)	Six Months Ended June 30, 2005	2004	Change (Points)
Combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion						
Claims and claim adjustment expense ratio	62.0%	66.1%	(4.1)	62.8%	65.4%	(2.6)
Underwriting expense ratio	32.4	32.7	(0.3)	31.9	32.6	(0.7)
Dividend ratio	1.0	1.1	(0.1)	0.9	0.9	-
Subtotal	95.4	99.9	(4.5)	95.6	98.9	(3.3)
Catastrophes:						
- Four hurricanes 2004	-	-	-	-	-	-
- All other	0.9	1.9	(1.0)	0.8	1.5	(0.7)
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other	0.7	(1.0)	1.7	0.3	(0.6)	0.9
Discount accretion	-	-	-	-	-	-
Total combined ratio[1]	97.0%	100.8%	(3.8)	96.7%	99.8%	(3.1)

1 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

RAM's combined ratio for the three and six months ended June 30, 2005 was 97.0% and 96.7%, respectively, representing decreases of 3.8 and 3.1 points from the same periods in 2004. The decrease in both periods primarily reflects the favorable impact of improved property results excluding catastrophes and underwriting and pricing actions taken. The decrease in the expense ratio reflects earned premium growth, which more than offset the growth in underwriting expenses. In addition, catastrophe losses decreased 1.0 and 0.7 points in the quarter and year-to-date, respectively, due to favorable weather across most regions. Partially offsetting these decreases was an increase in the amount of net incurred losses attributable to prior years related to commercial multiple peril and auto liability lines. The combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion was 95.4% and 95.6% in the quarter and year-to-date, respectively, representing decreases of 4.5 and 3.3 points from the comparable periods in 2004.

PTOI for the three and six months ended June 30, 2005 was $105 million and $210 million, respectively, representing increases of $43 million and $74 million over the same periods in 2004.

Federal and foreign income tax expense for the three and six months ended June 30, 2005 was $38 million and $75 million, respectively, representing increases of $16 million and $28 million over the same periods in 2004.

Net income for the three and six months ended June 30, 2005 was $70 million and $138 million, respectively, representing increases of $30 million and $51 million over the same periods in 2004.

INTERNATIONAL

(1) Overview – International

International net written premium by market segment was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
International local businesses	$553	$452	22.3%	$1,105	$921	20.0%
Liberty International Underwriters	370	385	(3.9)	829	865	(4.2)
Total net written premium	$923	$837	10.3%	$1,934	$1,786	8.3%

The Company's International operations provide insurance products and services through 1) local businesses, which sell personal and small commercial lines products and 2) Liberty International Underwriters ("LIU") which sells specialty commercial lines insurance and reinsurance products worldwide.

International's five major lines of business are as follows:

(1) Local businesses: personal and small commercial insurance;
(2) LIU reinsurance: includes multi-line insurance and reinsurance with an emphasis on property, treaty casualty, personal accident, aviation and reinsurance through Lloyd's Syndicate 4472 (formerly Lloyd's Syndicates 190 and 282);
(3) LIU third party: includes casualty, excess casualty, D&O, E&O and professional liability;
(4) LIU first party: includes marine, energy, engineering, aviation and property; and
(5) LIU other: includes workers compensation, commercial auto, and residual value.

International net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Local businesses	$553	$452	22.3%	$1,105	$921	20.0%
LIU reinsurance	198	218	(9.2)	469	508	(7.7)
LIU third party	113	92	22.8	207	173	19.7
LIU first party	52	68	(23.5)	126	158	(20.3)
LIU other	7	7	-	27	26	3.8
Total net written premium	$923	$837	10.3%	$1,934	$1,786	8.3%

NM = Not Meaningful

Net written premium for the three and six months ended June 30, 2005 was $923 million and $1.934 billion, respectively, representing increases of $86 million and $148 million over the same periods in 2004. Approximately $99 million and $174 million of the increase in the quarter and year-to-date, respectively, reflects growth in the Company's local operations in Europe and Latin America. Included in these amounts was approximately $11 million and $18 million of written premium in the quarter and year-to-date, respectively, related to the acquisitions of the Chilean operations of AGF Allianz Chile S.A in the third quarter of 2004 and ING Chile Seguros Generales in the second quarter of 2005. In addition, net written premium in LIU's third party segment increased $21 million and $34 million in the quarter and year-to-date, respectively, primarily due to a reduction in the Company's utilization of reinsurance as compared to the prior periods. Partially offsetting these increases was a decrease of $36 million and $71 million in the quarter and year-to-date, respectively, related to LIU's first party and reinsurance businesses in response to a less attractive rate environment. The reduction in LIU's reinsurance segment net written premium was in

part offset by $16 million and $32 million of accrued profit sharing related to ceded reinsurance estimated and accrued in the quarter and year-to-date, respectively. The inclusion of an estimated profit share reduced the amount of ceded written and earned premium in both periods.

(2) Results of Operations – International

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Revenues	$980	$891	10.0%	$1,879	$1,780	5.6%
PTOI before catastrophes, net incurred losses attributable to prior years and discount accretion	$81	$87	(6.9%)	$159	$196	(18.9%)
Catastrophes[1]:						
- Four hurricanes 2004	(30)	-	NM	(30)	-	NM
- All other	-	-	-	-	-	-
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other[2]	(1)	13	NM	(1)	(25)	(96.0)
Discount accretion	-	-	-	-	-	-
Pre-tax operating income	50	100	(50.0)	128	171	(25.1)
Realized investment (losses) gains, net	(2)	11	NM	(1)	11	NM
Federal and foreign income tax expense	(38)	(22)	72.7	(64)	(43)	48.8
Discontinued operations, net of tax	(3)	-	NM	(12)	-	NM
Extraordinary items, net of tax	-	-	-	-	-	-
Net income	$7	$89	(92.1%)	$51	$139	(63.3%)

1 The Company does not typically identify catastrophe losses from reinsurance assumed through Lloyd's Syndicate 4472 in the tables above given the expected volatility associated with property-reinsurance coverage. However, due to the significant impact that the four hurricanes had on the Company's results, these losses have been separately identified in the tables above. Catastrophe losses include the impact of reinstatement premiums.

2 Net of earned premium attributable to prior years of $2 million and $5 million for the three and six months ended June 30, 2005, respectively, and $3 million and $6 million for the comparable periods of 2004.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2005 were $980 million and $1.879 billion, respectively, representing increases of $89 million and $99 million over the same periods in 2004. The major components of revenues include net premium earned and net investment income.

Net premium earned for the three and six months ended June 30, 2005 was $883 million and $1.689 billion, respectively, representing increases of $88 million and $90 million over the same periods in 2004. Approximately $94 million and $179 million of the increase in the quarter and year-to-date, respectively, reflects growth in the Company's local operations in Europe and Latin America. Included in these amounts was approximately $12 million and $20 million of earned premium in the quarter and year-to-date, respectively, related to the acquisitions in Chile. In addition, net earned premium from LIU's third party segment also increased by $10 million in both periods. These increases were partially offset by decreases in LIU's first party and reinsurance segments of $13 million and $90 million in the quarter and year-to-date, respectively. LIU's reinsurance operations' written and earned premium require significant estimation throughout the year. The reduction in net premiums earned in the quarter and year-to-date is due to changes in estimates of written and earned premiums from prior periods and underlying changes in the exposure periods of the business written resulting from a change in business mix.

Net investment income for the three and six months ended June 30, 2005 was $90 million and $171 million, respectively, representing increases of $12 million and $16 million over the same periods in 2004.

This increase reflects a higher invested asset base and continued positive cash flow from operations, partially offset by lower investment yields.

Claims, benefits and expenses for the three and six months ended June 30, 2005 were $932 million and $1.752 billion, respectively, representing increases of $152 million and $154 million over the same periods in 2004. Approximately $69 million and $113 million of the increase in claim expenses in the quarter and year-to-date, respectively, was due to growth and a decrease in the amount of net favorable prior year development in 2005 versus 2004 related to the company's local businesses operations. Additionally, $30 million of the increase in claims expense in both periods was related to an increase in the estimate of incurred losses for the four hurricanes of 2004 as a result of delayed reporting of losses to the LIU reinsurance segment. In addition, underwriting expenses increased by $60 million and $101 million in the quarter and year-to-date, respectively, reflecting higher acquisition costs from organic growth in the local businesses, increased personnel costs related to business growth and the impact of foreign exchange. Foreign exchange added $13 million and $48 million in the quarter and year-to-date, respectively, versus the same periods in 2004. Partially offsetting these increases was a decrease in claims expense of $14 million and $78 million in the quarter and year-to-date, respectively, from LIU's first party and other segments associated with the reduction in business volumes and lower incurred losses attributable to prior years.

	Three Months Ended June 30,			**Six Months Ended June 30,**		
INTERNATIONAL	**2005**	**2004**	**Change (Points)**	**2005**	**2004**	**Change (Points)**
Combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion						
Claims and claim adjustment expense ratio	66.6%	67.5%	(0.9)	66.5%	66.7%	(0.2)
Underwriting expense ratio	31.0	28.9	2.1	30.7	29.2	1.5
Dividend ratio	-	-	-	-	-	-
Subtotal	97.6	96.4	1.2	97.2	95.9	1.3
Catastrophes[1]:						
- Four hurricanes 2004	3.6	-	3.6	1.9	-	1.9
- All other	-	-	-	-	-	-
Net incurred losses attributable to prior years:						
- Asbestos	-	-	-	-	-	-
- All other	0.1	(1.7)	1.8	-	1.6	(1.6)
Discount accretion	-	-	-	-	-	-
Total combined ratio	101.3%	94.7%	6.6	99.1%	97.5%	1.6

1 The Company does not typically identify catastrophe losses from reinsurance assumed through Lloyd's Syndicate 4472 in the tables above given the expected volatility associated with property-reinsurance coverage. However, due to the significant impact that the four hurricanes had on the Company's results, these losses have been separately identified in the tables above. Catastrophe losses include the impact of reinstatement premiums.

International's combined ratio for the three and six months ended June 30, 2005 was 101.3% and 99.1%, respectively, representing increases of 6.6 and 1.6 points over the same periods in 2004. The increase in the quarter and year-to-date reflects increases of 3.6 and 1.9 points, respectively, related to estimated losses from the 2004 hurricanes and increases of 2.1 and 1.5 points, respectively, related to the underwriting expense ratio due principally to increased personnel costs in LIU. The increase in the quarter is also due to a 1.8 point increase in net incurred losses attributable to prior years, principally related to a decrease in net favorable prior year development in the local businesses segment. The year-to-date results also reflect a 1.6 point decrease in net incurred losses attributable to prior years related to the non-recurrence of prior year development on LIU's business partially offset by a decrease in net favorable prior year development in the local businesses segment. The combined ratio before catastrophes, net incurred losses attributable to prior years and discount accretion was 97.6% and 97.2% in the quarter and year-to-date, respectively,

representing increases of 1.2 and 1.3 points over the comparable periods in 2004, primarily due to the higher expense ratio.

PTOI for the three and six months ended June 30, 2005 was $50 million and $128 million, respectively, representing decreases of $50 million and $43 million over the same periods in 2004.

Federal and foreign income taxes for the three and six months ended June 30, 2005 were $38 million and $64 million, respectively, representing increases of $16 million and $21 million over the same periods in 2004. Included in the second quarter 2005 income tax expense is a $22 million tax charge incurred for planned repatriation of profits under the American Jobs Creation Act of 2004 and $15 million of tax expense for prior year taxes resulting from a judicial decision in Brazil.

Net income for the three and six months ended June 30, 2005 was $7 million and $51 million, respectively, representing decreases of $82 million and $88 million from the same periods in 2004. Results from discontinued operations in the three and six months ended June 30, 2005 include losses of $3 million and $12 million, respectively, related to the disposal of certain pension business in Spain, which was part of the Genesis acquisition.

CORPORATE and OTHER

(1) Overview – Corporate and Other

Corporate and Other includes the following significant items:

- Individual Life, which provides life insurance and annuities for individuals and also issues structured settlement contracts and administers separate account contracts. Individual Life is licensed and sells its products in all 50 states, the District of Columbia and Canada.

- Certain discontinued operations, composed of the Company's asbestos, environmental, and toxic tort exposure and other internal discontinued operations, primarily the run-off of the California workers compensation business of Golden Eagle Insurance Corporation ("Golden Eagle").

- Interest expense on the Company's outstanding debt and gain or loss on extinguishment of debt.

- Internal reinsurance programs.

- Costs associated with certain long-term compensation plans and other corporate costs not allocated to the business units. In 2005, pension expense previously included in Corporate and Other was reallocated to the business segments. For consistency, 2004 has been restated to reflect the pension expense allocation. Domestic property and casualty operations' investment income was allocated based on planned ordinary investment income returns by investment category allocated to the strategic business units. Investments are allocated as follows: fixed income equal to liabilities net of insurance assets (reinsurance, premiums receivable, etc.) and a combination of fixed income, equity and nontraditional investments supporting allocated statutory policyholders' surplus. For internal reporting purposes, the Company allocates expected long-term returns on invested assets, including realized investment gains. Under this internal reporting view, the difference between actual investment income and allocated investment income is included in Corporate and Other.

- Federal and foreign income taxes represent the difference between the consolidated income tax expense and the amounts recognized by the Personal, Commercial, RAM and International segments. Domestic operations included in the segments reflect income tax at the 35% marginal U.S. Federal tax rate and do not reflect changes in the domestic valuation allowance (included in Corporate and Other), while the International segment reflects the actual tax expense of each country including changes in the international valuation allowance.

- Net income (loss) related to energy and non-energy related limited partnership investments.

- Substantially all realized gains (losses) from the domestic property-casualty investment portfolio.

- Fee and other revenues from the Company's wholly owned subsidiary, Liberty Energy Holdings, LLC ("Liberty Energy"). Liberty Energy generates revenue from the production and sale of oil and gas.

(2) Results of Operations – Corporate and Other

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2005**	**2004**	**Change**	**2005**	**2004**	**Change**
Revenues	$479	$232	106.5%	$766	$493	55.4%
Pre-tax operating income (loss) before catastrophes, net incurred losses attributable to prior years and discount accretion	$53	($1)	NM	$37	($13)	NM
Catastrophes:						
- Four hurricanes 2004	(6)	-	NM	(6)	-	NM
- All other	-	-	-	-	-	-
Net incurred losses attributable to prior years:						
- Asbestos	(2)	(4)	(50.0)	(2)	(4)	(50.0)
- All other	(31)	(41)	(24.4)	(75)	(93)	(19.4)
Discount accretion[1]	(2)	(3)	(33.3)	(5)	(6)	(16.7)
Pre-tax operating income (loss)[2]	12	(49)	NM	(51)	(116)	(56.0)
Realized investment gains, net	184	26	NM	204	85	140.0
Federal and foreign income tax benefit	46	128	(64.1)	201	226	(11.1)
Discontinued operations, net of tax	-	-	-	-	1	NM
Extraordinary items, net of tax	-	-	-	-	-	-
Net income	$242	$105	130.5%	$354	$196	80.6%

1 The Company discounts the long-term indemnity portion of its workers compensation claims as permitted by insurance regulations. The discount accretion on these claims is included in underwriting results as the loss reserves accrete to nominal value. Asbestos settlements are discounted at 4.5%.

2 In the first quarter of 2005, the Company changed its methodology for allocating qualified pension expenses. Historically, qualified pension expenses were recorded in the Corporate and Other segment but are now allocated to each of the Company's business units. Results for 2004 reflect this reclassification.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2005 were $479 million and $766 million, respectively, representing increases of $247 million and $273 million over the same periods in 2004. The major components of revenues include net premium earned, net investment income, net realized investment gains and losses and fee and other revenue.

Net premium earned for the three and six months ended June 30, 2005 was $52 million and $113 million, respectively, representing increases of $5 million and $20 million over the same periods in 2004. The increase is primarily due to earned premium on internal catastrophe reinsurance programs, partially offset by a decline in structured settlement sales. Internal reinsurance is provided to domestic businesses desiring catastrophe reinsurance below the corporate retention.

Net investment income for the three and six months ended June 30, 2005 was $197 million and $363 million, respectively, representing increases of $68 million and $116 million over the same periods in 2004. For the three and six months ended June 30, 2005, the increase in net investment income is primarily due to increases in limited partnership income of $42 million and $65 million respectively, as well as higher interest and dividend income due to a higher invested asset base as the Company continues to generate significant cash flow from operations, and the debt issuances of 2004 and 2005.

Realized investment gains for the three and six months ended June 30, 2005 were $184 million and $204 million, respectively, representing increases of $158 million and $119 million over the same periods in 2004. The increase reflects higher realized gains on fixed maturities, equities and energy investments and a reduction in impairment losses over the comparable periods in 2004.

Fee and other revenues for the three and six months ended June 30, 2005 were $46 million and $86 million, respectively, representing increases of $16 million and $18 million over the same periods in 2004, primarily due to the production and sale of oil and gas from Liberty Energy operations.

Claims, benefits and expenses for the three and six months ended June 30, 2005 were $283 million and $613 million, respectively, representing increases of $28 million and $89 million over the same periods in 2004. The increase in the quarter is primarily related to an increase in variable compensation and other benefit plans and interest expense related to the Company's March 2005 debt issuance. The increase year-to-date reflects increases in policyholder benefits related to discontinued variable annuity reinsurance business, variable compensation and other benefit plans, and interest expense related to the Company's March 2005 and 2004 debt issuances. Partially offsetting these increases was a decrease in incurred losses attributable to prior year of $13 million and $21 million in the quarter and year-to-date, respectively.

Pre-tax operating income (loss) for the three and six months ended June 30, 2005 was $12 million and ($51) million, respectively, representing improvements of $61 million and $65 million over the same periods in 2004. Corporate and Other recognized a Federal and foreign income tax benefit for the three and six months ended June 30, 2005 of $46 million and $201 million, respectively, representing decreases of $82 million and $25 million over the comparable periods in 2004. See the Consolidated Section for a discussion of taxes.

Net income for the three and six months ended June 30, 2005 was $242 million and $354 million, respectively, representing increases of $137 million and $158 million over the same periods in 2004.

INVESTMENTS

General

The Company's investment strategy seeks long-term returns through disciplined security selection, portfolio diversity and an integrated approach to risk management. The Company selects and monitors investments to balance the goals of safety, stability, liquidity, growth and after-tax total return with its need to comply with regulatory investment requirements. Diversity is achieved by maintaining a broadly based portfolio composed primarily of higher quality bonds, common stocks and limited partnerships (largely venture capital and leveraged buyout funds). These core holdings are supplemented by investments in additional asset types with the objective of further enhancing the portfolio's diversification and expected returns. These additional asset types include non-investment-grade bonds, foreign securities, limited partnerships including co-investments and direct investments in oil and gas ventures. Risk management is accomplished through asset liability management (including both interest rate risk and foreign currency risk), diversification, credit limits and a careful analytic review of each investment decision.

The Company's investment policy and strategy are reviewed and approved by the Investment Committee of its Board of Directors, which meets on a regular basis to review and consider investment activities, tactics and new investment classes. In addition, the Company has an experienced team of investment personnel responsible for managing and administering the investment portfolios of its domestic and foreign insurance operations.

Invested Assets

The following table summarizes the Company's invested assets by asset category at June 30, 2005 and December 31, 2004:

$ in Millions	**As of June 30, 2005**		**As of December 31, 2004**	
Invested Assets by Type	**Market Value**	**% of Total**	**Market Value**	**% of Total**
Fixed maturities, available for sale, at fair value	$37,024	91.3%	$35,601	90.0%
Equity securities, available for sale, at fair value	1,730	4.3	1,802	4.6
Trading securities, at fair value	189	0.5	457	1.2
Limited partnerships	907	2.2	881	2.2
Short-term investments	620	1.5	687	1.7
Other investments	90	0.2	109	0.3
Total invested assets	$40,560	100.0%	$39,537	100.0%

Total invested assets as of June 30, 2005 were $40.560 billion, a $1.023 billion or 2.6% increase over December 31, 2004. The increase in invested assets was primarily due to strong cash flow from operations of $1.747 billion and approximately $486 million of net proceeds from LMGI's March 22, 2005 debt offering. In addition, cash and cash equivalents temporarily increased $952 million or 36.7% from December 31, 2004. These funds will be tactically deployed in subsequent periods.

Fixed maturities as of June 30, 2005 were $37.024 billion, which represents an increase of $1.423 billion or 4.0% over December 31, 2004. The improvement reflects the aforementioned increase in the amount of available cash to invest and a higher amount of net unrealized gains in the portfolio due to the decrease in long-term interest rates during the period. Net unrealized gains on fixed maturities as of June 30, 2005 were $1.469 billion, a $147 million or 11.1% increase from December 31, 2004 primarily due to a decrease in long-term interest rates.

Equity securities as of June 30, 2005 were $1.730 billion, a $72 million or 4.0% decrease from December 31, 2004. This decrease was due primarily to the timing of foreign equity sales in conjunction with a

change in investment managers. The decline is expected to reverse in subsequent periods as the newly appointed manager reinvests in the sector.

Trading securities as of June 30, 2005 were $189 million, a $268 million or 58.6% decrease from December 31, 2004. The large decline was primarily attributable to the disposal of certain pension business in Spain, which was a part of the Genesis acquisition, and the partial liquidation of the Company's actively managed equity trading portfolio.

Limited partnerships as of June 30, 2005 were $907 million, a $26 million or 3.0% increase over December 31, 2004. The Company's investments in limited partnerships are long-term in nature and highly illiquid. The Company makes allocations to these investments because the Company believes that they offer the potential for superior long-term returns and are appropriate in the overall context of a diversified portfolio.

As of June 30, 2005, the Company had unfunded energy and non-energy commitments of $132 million and $633 million, respectively. At June 30, 2005, fixed maturities included commitments by the Company to purchase various mortgage-backed securities, at a cost of $207 million with a fair value of $208 million.

As of June 30, 2005, no single issuer accounted for more than 1.04% of invested assets.

The following tables summarize the Company's fixed income portfolio by security type, credit quality and maturity at June 30, 2005 and December 31, 2004:

$ in Millions	**As of June 30, 2005**		**As of December 31, 2004**	
Fixed Maturities by Security Type	**Market Value**	**% of Total**	**Market Value**	**% of Total**
U.S. Treasury securities	$ 3,195	8.6%	$ 2,703	7.6%
Mortgage and asset-backed securities	12,845	34.7	12,933	36.3
State and municipal	2,157	5.8	1,141	3.2
Corporate and other	15,209	41.1	15,033	42.2
Foreign	3,618	9.8	3,791	10.7
Total fixed maturities	$37,024	100.0%	$35,601	100.0%

During the first half of 2005, the Company, after consideration of investment opportunities, its tax status, and the current and prospective business environment, increased its tactical allocation in state and municipal and U.S. Treasury securities by $1.016 billion and $492 million, respectively.

$ in Millions	**As of June 30, 2005**		**As of December 31, 2004**	
Fixed Maturities by Credit Quality*	**Market Value**	**% of Total**	**Market Value**	**% of Total**
AAA	$19,949	54.0%	$19,265	54.1%
AA+, AA, AA-	3,231	8.7	2,889	8.1
A+, A, A-	7,301	19.7	6,977	19.6
BBB+, BBB, BBB-	3,918	10.6	4,124	11.6
BB+, BB, BB-	1,490	4.0	1,235	3.5
B+, B, B-	1,081	2.9	1,058	3.0
CCC or lower	54	0.1	53	0.1
Total fixed maturities	$37,024	100.0%	$35,601	100.0%

******For purposes of this disclosure, credit quality is primarily based upon Standard & Poor's ratings.*

The Company's allocation in investment grade bonds decreased slightly to 93.0% at June 30, 2005 from 93.4% at December 31, 2004. The decrease reflects the initiation of a syndicated bank loan investment program (approximately $106 million) and recent rating actions by Standard & Poor's on two issuers in the

automotive sector. The Company defines an investment grade bond as a security with a rating equivalent to the Standard and Poor's rating of BBB- or higher.

The remaining 7.0% of the Company's investments in fixed maturity securities are rated below investment grade. The Company's holdings of below investment grade securities primarily consist of: (1) a diversified portfolio of high yield bonds within the domestic insurance portfolios; (2) investments in individual emerging market sovereigns that support the Company's international insurance companies located in Argentina, Colombia and Venezuela; (3) the previously mentioned downgrades; and (4) the newly initiated investments in syndicated bank loans.

$ in Millions	As of June 30, 2005		As of December 31, 2004	
Fixed Maturities by Maturity Date	**Market Value**	**% of Total**	**Market Value**	**% of Total**
1 yr or less	$ 1,039	2.8%	$ 890	2.5%
Over 1yr through 5yrs	6,246	16.9	5,543	15.6
Over 5yrs through 10yrs	8,665	23.4	8,148	22.9
Over ten years	8,195	22.1	8,052	22.6
Mortgage and asset-backed securities	12,879	34.8	12,968	36.4
Total fixed maturities	$37,024	100.0%	$35,601	100.0%

During the first half of 2005, the Company did not make any significant change to the average life of its fixed maturity portfolio after taking into consideration changes in investment opportunities and its view of the current and prospective business and economic environment.

Net Investment Income

The following table summarizes the Company's net investment income at June 30, 2005 and 2004:

$ in Millions	Three Months Ended June 30,		Six Months Ended June 30,	
Net Investment Income	**2005**	**2004**	**2005**	**2004**
Interest income	$513	$492	$1,020	$960
Dividends	35	30	59	52
Limited partnerships	61	19	112	47
Other investment income	4	3	7	5
Gross investment income	613	544	1,198	1,064
Investment expenses	(20)	(24)	(50)	(42)
Net investment income	$593	$520	$1,148	$1,022

Net investment income for the three and six months ended June 30, 2005 was $593 million and $1.148 billion, respectively, representing increases of $73 million and $126 million over the same periods in 2004. The improvement reflects an increase of $21 million and $60 million in interest income in the quarter and year-to-date, respectively, primarily due to a higher invested asset base as the Company continues to generate significant cash flow from operations. In addition, the Company reported increases of $42 million and $65 million in the quarter and year-to-date, respectively, from limited partnership income related to private equity investments.

Net Realized Investment Gains (Losses)

The following tables summarize the Company's net realized investment gains (losses) at June 30, 2005 and 2004:

$ in Millions **Net Realized Investment Gains (Losses)**	Sales & Dispositions	Impairments	Change in Trading Security Unrealized	Total
Three Months Ended June 30, 2005:				
Fixed maturities	$70	$ -	$ -	$70
Common and preferred stock	47	(7)	7	47
Other	68	-	-	68
Total	$185	$(7)	$7	$185
Three Months Ended June 30, 2004:				
Fixed maturities	$59	$ -	$ -	$59
Common and preferred stock	(4)	(15)	-	(19)
Other	(3)	-	-	(3)
Total	$52	$(15)	$ -	$37
Six Months Ended June 30, 2005:				
Fixed maturities	$92	$ -	$ -	$92
Common and preferred stock	59	(8)	(7)	44
Other	70	-	-	70
Total	$221	$(8)	$(7)	$206
Six Months Ended June 30, 2004:				
Fixed maturities	$115	$ (5)	$ -	$110
Common and preferred stock	22	(24)	(8)	(10)
Other	(6)	-	-	(6)
Total	$131	$(29)	$(8)	$94

$ in Millions	Three Months Ended June 30,		Six Months Ended June 30,	
Components of Net Realized Investment Gains (Losses)	**2005**	**2004**	**2005**	**2004**
Fixed maturities:				
Gross realized gains	$75	$74	$109	$140
Gross realized losses	(5)	(15)	(17)	(30)
Equities:				
Gross realized gains	62	18	80	51
Gross realized losses	(15)	(37)	(36)	(61)
Other:				
Gross realized gains	69	1	71	1
Gross realized losses	(1)	(4)	(1)	(7)
Total net realized investment gains (losses)	$185	$37	$206	$94

Net realized investment gains for the three and six months ended June 30, 2005 were $185 million and $206 million, respectively, representing increases of $148 million and $112 million over the same periods in 2004. The improvement in the quarter reflects increases of $71 million in other investments primarily related to energy gains, $66 million in equities driven by gains on sales of foreign equities and private equity investments, and $11 million in fixed maturities. The improvement year-to-date reflects higher gains in equities and other investments of $54 million and $76 million, respectively, partially offset by a decrease in fixed maturities of $18 million. In addition, impairment losses decreased $8 million and $21 million in the quarter and year-to-date, respectively, from the comparable periods in 2004.

The following table shows a schedule of the Company's unrealized losses and fair value by security type by duration of potential impairment at June 30, 2005:

$ in Millions	Less Than 12 Months		Greater Than 12 Months	
Unrealized Losses & Fair Value by Security Type	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**
U.S. Treasury securities	$ (7)	$1,041	$ (5)	$ 152
Mortgage and asset-backed securities	(6)	908	(19)	969
State and municipal	(3)	314	(2)	78
Corporate and other	(47)	2,320	(22)	1,013
Foreign	(7)	220	(1)	52
Equities	(17)	139	(8)	45
Total	$(87)	$4,942	$(57)	$2,309

Unrealized losses decreased from $169 million as of December 31, 2004 to $144 million as of June 30, 2005 primarily due to a decrease in long-term interest rates. The Company frequently monitors the difference between the cost and estimated fair value of investments, which involves uncertainty as to whether declines in value are temporary in nature. The Company employs a systematic methodology to evaluate declines in fair values below amortized cost for all investments. The methodology utilizes a quantitative and qualitative process ensuring that available evidence concerning the declines in fair value below amortized cost is evaluated in a disciplined manner.

If the Company believes a decline in the value of a particular investment is temporary, the decline is recorded as an unrealized loss in shareholders' equity. If the decline is believed to be "other-than-

temporary," the carrying value of the investment is written down to market and a realized loss is recorded. As a result of this review, the Company has concluded that the gross unrealized losses of fixed maturity securities as of June 30, 2005 are temporary.

The gross unrealized losses recorded on common equity securities and other investments at June 30, 2005 resulted primarily from decreases in quoted market values from the dates that certain investment securities were acquired as opposed to fundamental changes in the issuer's financial performance and near-term financial prospects. Therefore, these decreases are also viewed as being temporary in accordance with the Company's policy with respect to recognizing impairments in the investment portfolio.

LIQUIDITY AND CAPITAL RESOURCES

General

The liquidity requirements of the insurance subsidiaries are met primarily by funds generated from operations, asset maturities and income received on investments. Cash provided from these sources is used primarily for claims, claim adjustment expenses and operating expenses (underwriting and corporate benefit costs). There are certain cash outflows such as catastrophes and continued settlements of asbestos reserves that are unpredictable in nature and could create increased liquidity needs. The Company believes that the insurance subsidiaries' future business liquidity needs will be met from all the above sources.

Net cash flows are generally invested in marketable securities. The Company invests its net cash flows in fixed income securities and equities while keeping a certain amount in cash and short-term investments to meet unpredictable cash obligations. For ongoing business, the Company monitors the duration of these investments, and purchases and sales are executed with the objective of having adequate cash available to satisfy its maturing liabilities. As the Company's investment strategy focuses on overall asset and liability durations, and not specific cash flows, asset sales may be required to satisfy obligations or rebalance asset portfolios. The Company's invested assets as of June 30, 2005 totaled $40.560 billion.

Short-term debt outstanding at June 30, 2005 and December 31, 2004 was as follows:

$ in Millions	**As of June 30, 2005**	**As of December 31, 2004**
Commercial paper	$ -	$147
Revolving credit facilities	29	29
Current maturities of long-term debt	-	77
Total short-term debt	$29	$253

Long-term debt outstanding at June 30, 2005 and December 31, 2004 was as follows:

$ in Millions	**As of June 30, 2005**	**As of December 31, 2004**
8.20% Surplus notes, due 2007	$121	$121
6.75% Notes, due 2008	15	15
5.00% Prudential notes due 2008	14	14
8.00% Prudential notes—series B due 2013	260	260
5.75% Senior notes, due 2014	500	500
8.50% Surplus notes, due 2025	150	150
7.875% Surplus notes, due 2026	250	250
7.63% Notes, due 2028	3	3
7.00% Senior notes, due 2034	250	250
6.50% Senior notes, due 2035	500	-
7.697% Surplus notes, due 2097	500	500
7.10% – 7.86%, Medium term notes, with various maturities	27	27
Subtotal	2,590	2,090
Unamortized discount	(26)	(16)
Total long-term debt excluding current maturities	$2,564	$2,074

LMGI entered into a new $750 million five-year revolving credit agreement, which became effective on July 25, 2005. This agreement replaced the Company's previous credit facility ($450 million 364-day). The facility supports LMGI's $600 million commercial paper program and is available to provide working

capital to the Company's domestic insurance companies. The five-year credit agreement is guaranteed by LMIC. To date, no funds have been borrowed under the facility.

The Company also has a Venezuelan subsidiary, Inversora Segucar, C.A., which has entered into a revolving credit facility to provide liquidity for working capital purposes. Inversora Segucar also has short-term loans outstanding. As of June 30, 2005, total short-term loans and borrowings under the Venezuelan credit facility were approximately $29 million.

The $224 million decrease in short-term debt outstanding is primarily due to the redemption of $147 million of commercial paper, $61 million of maturing medium term notes and $16 million of 5% notes due in 2008 to Prudential Financial Inc. issued in connection with the PruPac acquisition.

The $490 million increase in long-term debt outstanding is primarily the result of the March 22, 2005 offering by LMGI of $500 million of 30-year senior notes. The proceeds were contributed to its wholly owned subsidiaries, LMIC and Employers Insurance Company of Wausau ("EICOW").

Consolidated interest expense for the three and six months ended June 30, 2005 was $48 million and $89 million, respectively, representing increases of $6 million and $12 million over the same periods in 2004. The increase is primarily due to the March 2004 and 2005 debt offerings.

Holding Company Liquidity and Capital Resources

The Company conducts substantially all of its operations through its wholly owned insurance and service company subsidiaries, and therefore is primarily dependent on dividends, distributions, loans or other payments of funds from these entities to meet its current and future obligations. However, the subsidiaries are separate and distinct legal entities and have no obligation to make funds available to the Company, whether in the form of loans, dividends or other distributions. As of June 30, 2005, the Company, through its downstream subsidiary LMGI, had $1.532 billion of debt outstanding.

The insurance subsidiaries ability to pay dividends is restricted under applicable insurance law and regulations. Under the insurance laws of the domiciliary states of the insurance subsidiaries, an insurer may make an ordinary dividend payment if its surplus as regards to policyholders, following such dividend, is reasonable in relation to its outstanding liabilities and adequate to its financial needs. However, no insurer may pay an extraordinary dividend without the approval or non-disapproval of the domiciliary insurance regulatory authority. Under the insurance laws of Massachusetts, the domiciliary state of LMIC and Liberty Mutual Fire Insurance Company ("LMFIC"), an extraordinary dividend is defined as a dividend whose fair market value, together with other dividends made within the preceding 12 months, exceeds the greater of 10% of the insurer's surplus as regards policyholders as of the preceding December 31, or the insurer's net income for the 12-month period ending on the preceding December 31. Under the insurance laws of Wisconsin, the domiciliary state of EICOW, an extraordinary dividend is defined as a dividend whose fair market value, together with other dividends paid within the preceding 12 months, exceeds the lesser of (a) 10% of the insurer's surplus as regards policyholders as of the preceding December 31, or (b) the greater of (1) the insurer's net income for the preceding calendar year, minus realized capital gains for that calendar year, or (2) the aggregate of the insurer's net income for the three preceding calendar years minus realized capital gains for those calendar years and minus dividends paid within the first two of the preceding three calendar years. Changes in the extraordinary dividend regulation of the domiciliary states of LMIC, LMFIC and EICOW could negatively affect LMGI's ability to pay principal and interest on the Notes, as could a redomestication, merger or consolidation of LMIC, LMFIC or EICOW to a different domiciliary state. Additionally, in connection with the Company's reorganization in 2001 into a mutual holding company structure, the Company entered into Keep Well Agreements with the Massachusetts Commissioner of Insurance, LMIC, LMFIC and certain other affiliates which effectively limit LMIC and LMFIC from paying any dividends to the Company when the "total adjusted capital" of the respective insurer is below 300% of the "authorized control level," as such terms are defined in the Massachusetts risk-based capital regulations as of June 13, 2001. The Keep Well Agreements will terminate automatically upon the earlier of (i) the date that is five years from the effective date of the respective reorganization (November 28, 2006 as to LMIC and March 19, 2007 as to LMFIC), or (ii) the date upon which the

Company, the respective insurer or LMHC Massachusetts Holdings Inc. becomes subject to the public reporting requirements of the Securities and Exchange Commission.

As of December 31, 2004, the authorized control level risk-based capital and 2005 dividend capacity prior to needing regulatory approval for LMIC, LMFIC and EICOW were as follows:

$ in Millions	**RBC Ratio [1]**			**Dividend Capacity[2]**
RBC Ratios and Dividend Capacity	**2004**	**2003**	**Change**	**2005**
LMIC	459%	360%	99 points	$726
LMFIC	473%	425%	48 points	$67
EICOW	346%	303%	43 points	$84

Note: In the first quarter of 2005, the Company made certain intercompany pooling reclassifications among its legal entities. These reclassifications had no impact on Consolidated Statutory or GAAP financial results, but did have an immaterial impact on the RBC ratio and dividend capacity of LMIC, LMFIC and EICOW from what the Company reported in the Q4 2004 MD&A.
[1] Authorized control level risk-based capital as defined by the NAIC.
[2] Represents maximum allowable dividend without prior regulatory approval in the state of domicile.

In addition, management expects the Company's subsidiary, Liberty Corporate Services LLC (the "service companies") to generate approximately $150 million of funding, which would be available to service the holding company obligations of LMGI in 2005. The service companies, which include Helmsman Insurance Agency, Summit Consulting and Helmsman Management Services, collect fees and other revenues for claims administration and agency services rendered for affiliated and non-affiliated insurance entities.

Statutory Surplus
Statutory surplus as regards policyholders for the combined operations of LMIC and its U.S. affiliates was $9.867 billion and $8.739 billion at June 30, 2005, and December 31, 2004, respectively. The increase in surplus in the first six months of 2005 is primarily due to $599 million of net income and $486 million of capital contributions related to the March 2005 debt offering. The balance of the increase in statutory surplus primarily reflects changes in affiliated and unaffiliated unrealized gains, deferred taxes, foreign exchange and non-admitted assets.

CRITICAL ACCOUNTING POLICIES

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the Company 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 financial statements, and the reported amounts of revenues and expenses during the reporting period. The Company's principal estimates include:

- unpaid claims and claim adjustment expense reserves, including asbestos and environmental liability reserves and recoverables on premium attributable to prior years;
- reinsurance recoverables, including bad debt provision;
- impairments to the fair value of the investment portfolio;
- the valuation of goodwill;
- deferred acquisition costs; and
- deferred income tax valuation allowance.

While the Company believes the amounts included in the consolidated financial statements reflect best estimates and appropriate assumptions, these amounts could ultimately be materially different from the amounts currently provided for in the consolidated financial statements.

Certain reclassifications have been made to the 2004 tables to conform to the 2005 tables.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were $34.655 billion and $33.884 billion at June 30, 2005 and December 31, 2004, respectively. The increase was due to growth less the on-going settlement of claims and incurred losses attributable to prior years including discount accretion. For the six months ended June 30, 2005 and 2004, incurred losses attributable to prior years including discount accretion and prior year losses related to the four hurricanes of 2004 were $184 million and $244 million, respectively.

Property-casualty insurance unpaid claims and claim adjustment expenses represent the Company's best estimate of amounts necessary to settle all outstanding claims, including claims that are incurred but not reported as of the reporting date. The Company's reserve projections are based primarily on detailed analysis of the facts in each case, experience with similar cases and various historical development patterns. Consideration is given to such historical patterns as field reserving trends and claims settlement practices, loss payments, pending levels of unpaid claims and product mix, as well as court decisions, economic conditions and public attitudes. All of these factors can affect the estimation of reserves.

Establishing loss reserves, including loss reserves for catastrophic events that have occurred, is an estimation process. Many factors can ultimately affect the final settlement of a claim and, therefore, the necessary reserve. Changes in the law, results of litigated cases, medical costs, and cost of repair materials and labor rates can all affect ultimate claim costs. In addition, the span of time between the incidence of a loss and the payment or settlement of the claim can be a critical part of reserving determinations and will cause more variability in the ultimate claim cost. Accordingly, "short-tail" claims, such as property damage claims, tend to be easier to estimate than "long-tail" claims, such as workers compensation or general liability claims.

As information develops that varies from past experience, provides additional data, or in some cases, augments data that previously was not considered sufficient for use in determining reserves, changes in the Company's estimate of ultimate liabilities may be required. The effects of these changes are reflected in current operating results.

Asbestos and Environmental

The Company's asbestos and environmental (A&E) reserves for unpaid claims and claim adjustment expenses were $1.528 billion and $1.641 billion at June 30, 2005 and December 31, 2004, respectively, net of reinsurance and including the related allowance for doubtful accounts. More than one-third of the decrease in A&E reserves was related to the resolution of environmental claims with a single policyholder. The remainder of the decrease relates to other A&E settlement activity during 2005.

All A&E claims against policies issued prior to 1986 by EICOW and its affiliates are 100% ceded to Nationwide Indemnity Company and guaranteed by Nationwide Mutual Insurance Company. The Company's 2003 acquisition of PruPac included $175 million and $118 million of gross and net asbestos reserves, respectively. Any increase in asbestos reserves is reinsured by Vantage Casualty Insurance Company and guaranteed by Prudential Financial Inc.

Some of the Company's loss reserves are for asbestos and environmental claims and related litigation. While the estimation of asbestos claims and associated liabilities and the analysis of environmental claims considered prevailing applicable law and certain inconsistencies of court decisions as to coverage, plaintiffs' expanded theories of liability, and the risks inherent in major litigation and other uncertainties, the Company believes that in future periods it is possible that the outcome of the continued uncertainties regarding asbestos and environmental related claims could result in liability that differs from current reserves by an amount that could be material to the Company's future operating results and financial condition.

Reinsurance Recoverables

The Company reported reinsurance recoverables of $14.695 billion and $14.209 billion at June 30, 2005 and December 31, 2004, respectively, net of allowance for doubtful accounts of $346 million and $349 million, respectively. The majority of the increase reflects growth in Liberty International Underwriters and increased cessions to state mandated involuntary pools and associations, offset by a decrease in cessions to Nationwide Indemnity Co.

The reinsurance recoverables from Nationwide Indemnity Co. have been fully guaranteed by its parent, Nationwide Mutual Insurance Co., which has a financial strength rating of A+ from Standard & Poor's and A+ from A.M. Best. The majority of reinsurance recoverables from state mandated involuntary pools and associations represent the Company's servicing carrier business. As a servicing carrier, the Company retains no direct underwriting risk but instead cedes 100% of the involuntary market premium and losses back to the pool. Payment of losses is shared by the pool participants in proportion to their pool participation. Credit risk with respect to this servicing carrier business is the composite of the cumulative creditworthiness of all participants in their respective pools.

As part of its reinsurance security oversight, the Company has established a Standing Reinsurance Credit Committee (SRC) that meets quarterly to monitor and review the credit quality of the existing reinsurance portfolio, discuss emerging trends in the reinsurance marketplace and ensure that the current portfolio of reinsurance is in compliance with the committee's security standards. The SRC is directly responsible for establishing the rating, collateral and diversification requirements governing the Company's purchase and use of reinsurance.

Approximately 94% of the Company's reinsurance recoverable balance, net of collateral held and including voluntary and involuntary pools and associations, was placed with reinsurers rated A- or better from A.M. Best at June 30, 2005. Collateral held against outstanding reinsurance recoverable balances was $3.737 billion and $3.589 billion at June 30, 2005 and December 31, 2004, respectively.

The remaining 6% of the Company's reinsurance recoverable balance is well diversified. With the exception of Converium, no single reinsurer rated B++ or below accounts for more than 1% of policyholder surplus. The average reinsurance recoverable balance of the remaining 6% is approximately $1 million as of June 30, 2005.

Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured business. The Company evaluates and monitors the financial condition of its reinsurers under voluntary reinsurance arrangements to minimize its exposure to significant losses from reinsurer insolvencies. The Company reports its reinsurance recoverables net of an allowance for estimated uncollectible reinsurance recoverables. The allowance is based upon the Company's ongoing review of amounts outstanding, length of collection periods, changes in reinsurer credit standing and other relevant factors. Accordingly, the establishment of reinsurance recoverables and the related allowance for uncollectible reinsurance recoverables is also an inherently uncertain process involving estimates. Changes in these estimates could result in additional income statement charges.

The Company is party to retroactive reinsurance arrangements where a significant portion of the consideration was retained on a "funds held" basis and interest is credited on the balance at a weighted average rate of approximately 7.7% annually. These contracts resulted in deferred gains (including experience related profit accruals of $195 million as of June 30, 2005 and December 31, 2004) that are amortized into income using the effective interest method over the estimated settlement periods. During the second quarter of 2005, the Company re-estimated the amount of deferred gains and amortization related to these reinsurance agreements. At June 30, 2005 and December 31, 2004, deferred gains related to these reinsurance arrangements (including the retroactive component of the program discussed below) were $943 million and $973 million, respectively, and are included in other liabilities within the consolidated balance sheets. Interest credited to the funds held balances for the three months and six months ended June 30, 2005 was $37 million and $61 million, respectively, as compared to $34 million and $57 million, for the three months and six months ended June 30, 2004, respectively. Amortization of the deferred gain for the three months and six months ended June 30, 2005 was $46 million and $58 million, respectively, as compared to $12 million and $23 million for the three months and six months ended June 30, 2004, respectively. Reinsurance recoverables related to these transactions including experience related profit accruals were $2.262 billion and $2.219 billion as of June 30, 2005 and December 31, 2004, respectively.

Additionally, the Company has an aggregate stop loss program covering substantially all of Commercial Markets voluntary workers compensation business from the fourth quarter 2000 through the fourth quarter 2002 accident year periods. Under these contracts, losses in excess of a specified loss ratio are reinsured up to a maximum loss ratio and were accounted for as prospective reinsurance at inception. However, due to a negotiated amendment to the 2000 contract at the January 1, 2002 renewal, premium and loss activity subsequent to December 31, 2001 is now accounted for as retroactive reinsurance for coverage provided from the fourth quarter 2000 through the fourth quarter 2001 covered accident year periods. Approximately $38 million and $31 million of additional losses were ceded to these retroactive and prospective contracts for the three months and six months ended June 30, 2005, with additional premium of $24 million and $22 million, respectively. Approximately $68 million and $78 million of additional losses were ceded to these retroactive and prospective contracts for the three months and six months ended June 30, 2004, with additional premium of $38 million and $45 million, respectively. The income statement impact of ceding the additional losses and premium on the fourth quarter 2000 through fourth quarter 2001 covered accident period was deferred for GAAP purposes and is amortized into income using the effective interest method over the estimated settlement period.

Impairment Losses on Investments

The total impairment losses on investments for the three and six months ended June 30, 2005 were $7 million and $8 million, respectively, representing an $8 million and $21 million decrease from the same periods in 2004. Unrealized losses that are other-than-temporary are recognized as realized losses. The Company's accounting policy for other-than-temporary impairment recognition requires other-than-

temporary impairment charges to be recorded when it is determined that the Company is unlikely to recover its cost basis in an investment in the near-term. Factors considered in evaluating whether a decline in value is other-than-temporary include: (a) the length of time and extent to which the fair value has been below cost; (b) the financial condition and near-term prospects of the issuer; and (c) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for any anticipated recovery. In addition, for securities expected to be sold, an other-than-temporary impairment charge is recognized if the Company does not expect the fair value of a security to recover to cost or amortized cost prior to the expected date of sale.

The Company employs a systematic methodology to evaluate declines in fair value below the book value for equity securities and other investments. The methodology utilizes a quantitative and qualitative process ensuring that available evidence concerning the declines in fair value below carrying value is evaluated in a disciplined manner. Based on that evaluation and the Company's ability and intent to hold these investments for a reasonable period of time sufficient for a recovery of fair value, the Company views the decline in market value of these investments as being temporary in accordance with the Company's impairment policy.

Variable Interest Entities

In January 2003, the FASB issued Interpretation No. 46, "*Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51*" ("FIN 46"). FIN 46 requires certain variable interest entities ("VIEs") to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or the entity does not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 was revised in late 2003 (FIN 46(R)) and was effective January 1, 2004 for the Company for all new VIEs created or acquired after December 31, 2003. For VIEs created or acquired by the Company prior to December 31, 2003, the provisions of FIN 46 have been applied in 2005.

The Company's primary exposure to FIN 46 VIEs, relates to investments in venture capital and private equity limited partnerships that are accounted for under the equity method. The Company has determined that it is the primary beneficiary for four VIEs with total assets of approximately $30 million at June 30, 2005. The Company's participation in the VIEs in which it is the primary beneficiary ranges from 66.49% to 99.99%. These assets are reflected as a component of other invested assets on the Company's consolidated balance sheets. The Company's maximum exposure to losses from these VIEs is approximately $29 million at June 30, 2005, and there is no recourse provision to the general credit of the Company beyond the full amount of the Company's loss exposure. The Company has investments in 15 VIEs for which it is not the primary beneficiary at June 30, 2005. The cumulative assets of these VIEs is $5.925 billion at June 30, 2005, of which the Company's maximum exposure was $297 million.

Goodwill and Intangibles

Goodwill and intangible assets were $806 million and $824 million at June 30, 2005 and December 31, 2004, respectively.

Deferred Policy Acquisition Costs

Total deferred policy acquisition costs were $1.425 billion and $1.354 billion as of June 30, 2005 and December 31, 2004, respectively. Deferred policy acquisition costs are costs that vary with, and are primarily related to, the acquisition of new and renewal insurance and investment contracts that are deferred and amortized over the respective policy terms. Deferred acquisition costs are reviewed annually for recoverability. Investment income is considered in the recoverability assessment. For short-duration insurance contracts, acquisition costs include commissions, underwriting expenses, and premium taxes and assessments. For long-duration insurance contracts, these costs include first year commissions in excess of annual renewal commissions and variable sales, underwriting and administrative expenses.

Deferred Income Taxes

The net deferred income tax asset was $1.037 billion and $938 million as of June 30, 2005 and December 31, 2004, respectively, net of a valuation allowance of $84 million and $340 million, respectively. Management believes it is more likely than not that the Company's net deferred tax assets will be realized based on the Company's ability and likelihood of generating future taxable income. The increase in the Company's net deferred income tax asset is the result of a reduction in the remaining domestic tax valuation allowance to zero during the quarter ended June 30, 2005, partially offset by deferred tax expense related to operating activities.

The income tax provision is calculated under the liability method. Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax bases of assets and liabilities at the enacted tax rates. The principal assets and liabilities giving rise to such differences are unrealized capital gains and losses on certain investments, insurance loss reserves, unearned premiums, deferred policy acquisition costs, employee benefits, net operating loss carryforwards and alternative minimum tax credits.

The Company provides for Federal and foreign income taxes based on amounts that it believes it ultimately will owe. Inherent in the provision for Federal and foreign income taxes are estimates regarding the deductibility of certain expenses and the realization of certain tax credits. In the event the ultimate deductibility of certain expenses or the realization of certain tax credits differs from estimates, the Company may be required to significantly change the provision for Federal and foreign income taxes recorded in the consolidated financial statements.

The American Jobs Creation Act of 2004 (the "Act") introduced a special one-time 85% dividends received deduction on the repatriation of certain foreign earnings to a United States taxpayer, provided certain criteria are met. The maximum amount of foreign earnings eligible for the deduction is limited to the greater of $500 million or the amount shown in the Company's most recent audited financial statements filed prior to June 30, 2003 as earnings permanently reinvested outside of the United States. Although the deduction is subject to a number of limitations and, as of today, some uncertainty remains as to how to interpret certain provisions in the Act, the Company believes that it has the information necessary to make an informed decision regarding the impact of the Act on its repatriation plans. Based on that decision, the Company plans to repatriate $196 million in extraordinary dividends, as defined in the Act, during 2005 and accordingly has recorded a tax liability of $22 million for such dividends during the quarter ending June 30, 2005. It is reasonably possible that the Company may repatriate some additional amount between $0 and $85 million beyond the $196 million, with the respective tax liability ranging from $0 to $4 million. The Company expects to be in a position to finalize its assessment of any additional repatriation amount during the quarter ending September 30, 2005. The Company has not provided for U.S. deferred income taxes or foreign withholding tax on basis differences in its non-U.S. subsidiaries of $327 million that result primarily from undistributed earnings the Company intends to reinvest indefinitely. Determination of the deferred income tax liability on these basis differences is not practicable because such liability, if any, is dependent on circumstances existing if and when remittance occurs.

About the Company

Boston-based Liberty Mutual Holding Company Inc., the parent corporation of the Liberty Mutual Group of entities ("LMG" or the "Company"), is a diversified global insurer and sixth largest property and casualty insurer in the U.S. based on 2004 direct written premium. The Company also ranks 111th on the Fortune 500 list of largest corporations in the United States based on 2004 revenue. As of December 31, 2004, LMG had $72.4 billion in consolidated assets and $19.6 billion in annual consolidated revenue.

LMG, through its subsidiaries and affiliated companies, offers a wide range of property-casualty insurance products and services to individuals and businesses alike. In 2001 and 2002, the Company formed a mutual holding company structure, whereby the three principal mutual insurance companies, LMIC, LMFIC and EICOW, each became separate stock insurance companies under the ownership of Liberty Mutual Holding Company.

Functionally, the Company conducts its business through four strategic business units: Personal Market, Commercial Markets, Agency Markets (formerly Regional Agency Markets) and International. Each business unit operates independently of the others and has dedicated sales, underwriting, claims, actuarial, financial and certain information technology resources. Management believes this structure allows each business unit to execute its business strategy and/or to make acquisitions without impacting or disrupting the operations of the Company's other business units.

LMG employs over 38,000 people in nearly 900 offices throughout the world. For a full description of the Company's business operations, products and distribution channels please visit the Liberty Mutual's Investor Relations web site at www.libertymutual.com/investors.