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

Quarter Ended March 31, 2012

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 "LMHC"), for the three months ended March 31, 2012 and 2011. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's December 31, 2011 Audited Consolidated Financial Statements, March 31, 2012 Unaudited Consolidated Financial Statements and First Quarter 2012 Financial Supplement located on the Company's Investor Relations website at www.libertymutual.com/investors. The Company's discussions related to net income are presented in conformity with U.S. generally accepted accounting principles ("GAAP") on an after-tax 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.

Some of the factors that could cause actual results to differ include, but are not limited to the following: the occurrence of catastrophic events (including terrorist acts, hurricanes, hail, tornadoes, tsunamis, earthquakes, floods, snowfall and winter conditions); inadequacy of loss reserves; adverse developments involving asbestos, environmental or toxic tort claims and litigation; adverse developments in the cost, availability or ability to collect reinsurance; disruptions to the Company's relationships with its independent agents and brokers; financial disruption or a prolonged economic downturn; the performance of the Company's investment portfolios; a rise in interest rates; risks inherent in the Company's alternative investments in private limited partnerships ("LP") and limited liability companies ("LLC"); difficulty in valuing certain of the Company's investments; subjectivity in the determination of the amount of impairments taken on the Company's investments; unfavorable outcomes from litigation and other legal proceedings, including the effects of emerging claim and coverage issues and investigations by state and federal authorities; the Company's exposure to credit risk in certain of its business operations; terrorist acts; the Company's inability to obtain price increases or maintain market share due to competition or otherwise; inadequacy of the Company's pricing models; changes to insurance laws and regulations; changes in the amount of statutory capital that the Company must hold to maintain its financial strength and credit ratings; regulatory restrictions on the Company's ability to change its methods of marketing and underwriting in certain areas; assessments for guaranty funds and mandatory pooling arrangements; a downgrade in the Company's claims-paying and financial strength ratings; the ability of the Company's subsidiaries to pay dividends to the Company; inflation, including inflation in medical costs and automobile and home repair costs; the cyclicality of the property and casualty insurance industry; political, legal, operational and other risks faced by the Company's international business; potentially high severity losses involving the Company's surety products; loss or significant restriction on the Company's ability to use credit scoring in the pricing and underwriting of personal lines policies; inadequacy of the Company's controls to ensure compliance with legal and regulatory standards; changes in federal or state tax laws; risks arising out of the Company's securities lending program; the Company's utilization of information technology systems and its implementation of technology innovations; difficulties with technology or data security; insufficiency of the Company's business continuity plan in the event of a disaster; the Company's ability to successfully integrate operations, personnel and technology from its acquisitions; insufficiency of the Company's enterprise risk management models and modeling techniques; and changing climate conditions. 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 website 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 Consolidated Financial Statements.

Three Months Ended March 31, 2012 - Consolidated Results of Operations

- Revenues for the three months ended March 31, 2012 were $8.881 billion, an increase of $500 million or 6.0% over the same period in 2011.
- Net written premium ("NWP") for the three months ended March 31, 2012 was $8.078 billion, an increase of $495 million or 6.5% over the same period in 2011.
- Pre-tax operating income ("PTOI") before LP and LLC income for the three months ended March 31, 2012 was $456 million, an increase of $219 million or 92.4% over the same period in 2011.
- PTOI for the three months ended March 31, 2012 was $577 million, an increase of $130 million or 29.1% over the same period in 2011.
- Net income attributable to LMHC for the three months ended March 31, 2012 was $459 million, an increase of $95 million or 26.1% over the same period in 2011.
- Cash flow from operations for the three months ended March 31, 2012 was $651 million, an increase of $29 million or 4.7% over the same period in 2011.
- The consolidated combined ratio before catastrophes[1] and net incurred losses attributable to prior years[2] for the three months ended March 31, 2012 was 96.0%, a decrease of 0.9 points from the same period in 2011. Including the impact of catastrophes and net incurred losses attributable to prior years, the Company's combined ratio for the three months ended March 31, 2012 decreased 1.5 points to 100.9%.

Financial Condition as of March 31, 2012

- Total assets were $115.918 billion as of March 31, 2012, a decrease of $1.213 billion from December 31, 2011.
- Total equity was $18.504 billion as of March 31, 2012, an increase of $640 million over December 31, 2011.

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[1]Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

[2]Net incurred losses attributable to prior years is defined as incurred losses attributable to prior years (excluding prior year losses related to natural catastrophes) including both earned premium attributable to prior years and amortization of retroactive reinsurance gains.

Subsequent Events

- On April 18, 2012, the Company announced the commencement of two tender offers. The first offer is a cash tender offer to purchase up to $350,000,000, subject to increase, of the aggregate principal amount of Liberty Mutual Group, Inc.'s ("LMGI") 10.75% Series C Junior Subordinated Notes due 2088 and LMIC's 7.697% Surplus Notes due 2097, each at a purchase price determined in accordance with the procedures of a modified "Dutch Auction." The second offer is a cash tender offer by LMGI to purchase up to $350,000,000, subject to increase, of the aggregate principal amount of its 5.75% Senior Notes due 2014 and its 7.30% Senior Notes due 2014, each at a price determined by reference to a fixed spread above the bid-side yield on the applicable reference security (the "Waterfall Offer") and accepted in accordance with the acceptance priority level set forth in the tender documents. The Waterfall Offer is conditioned on LMGI issuing at least $350,000,000 aggregate principal amount of new senior notes. Unless extended or earlier terminated by the issuers, the tender offers will expire at 11:59 p.m., New York City time, on May 15, 2012.

CONSOLIDATED RESULTS OF OPERATIONS

The Company has identified consolidated PTOI and PTOI before LP and LLC income as non-GAAP financial measures. PTOI is defined by the Company as pre-tax income excluding net realized gains, loss on extinguishment of debt, extraordinary items, discontinued operations, integration and other acquisition related costs and cumulative effects of changes in accounting principles. PTOI before LP and LLC income is defined as PTOI excluding LP and LLC results recognized on the equity method. PTOI before LP and LLC income and PTOI are considered by the Company to be appropriate indicators of underwriting and operating results and are consistent with the way the Company internally evaluates performance. Net realized gains and LP and LLC results are significantly impacted by both discretionary and economic factors and are not necessarily indicative of operating results, and the timing and amount of integration and other acquisition related costs and the extinguishment of debt are not connected to the management of the insurance and underwriting aspects of the Company's business. Income taxes are significantly impacted by permanent differences. References to "direct written premium" represent the amount of premium recorded for policies issued during a fiscal period excluding assumed and ceded reinsurance. References to NWP represent the amount of premium recorded for policies issued during a fiscal period including audits, retrospectively rated premium related to loss sensitive policies, and assumed premium, less ceded premium. Assumed and ceded reinsurance premiums include premium adjustments for reinstatement of coverage when a loss has used some portion of the reinsurance provided, generally under catastrophe treaties ("reinstatement premium"). In addition, the majority of workers compensation premium is adjusted to the "booked as billed" method through the Corporate & Other segment. The Company believes that NWP is a performance measure useful to investors as it generally reflects current trends in the Company's sale of its 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.

Overview – Consolidated

Consolidated NWP by significant line of business was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Private passenger automobile	$2,728	$2,510	8.7%
Workers compensation	1,001	1,053	(4.9)
Homeowners	757	670	13.0
Commercial multiple peril / fire	633	606	4.5
International local businesses (excluding private passenger automobile)	595	517	15.1
Lloyd's Syndicate 4472	560	515	8.7
Commercial automobile	361	349	3.4
General liability	322	332	(3.0)
LIU[1] third party	238	185	28.6
Group disability and life	196	207	(5.3)
Surety	172	189	(9.0)
LIU inland marine program	108	96	12.5
Individual life	85	69	23.2
LIU first party	72	71	1.4
Other[2] (including AVR)	250	214	16.8
Total NWP[3]	$8,078	$7,583	6.5%

1 Liberty International Underwriters ("LIU").
2 Primarily includes NWP from assumed voluntary reinsurance ("AVR"), allied lines and domestic inland marine.
3 NWP associated with internal reinsurance has been re-allocated to the appropriate lines of business.

Consolidated NWP by SBU was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Liberty Mutual Agency Corporation ("LMAC")	$2,576	$2,503	2.9%
International	2,229	1,990	12.0
Personal Markets	1,846	1,675	10.2
Commercial Markets	1,545	1,589	(2.8)
Corporate and Other	(118)	(174)	(32.2)
Total NWP	$8,078	$7,583	6.5%
Foreign exchange effect on growth			(0.6%)
NWP growth excluding foreign exchange			7.1%

Major drivers of NWP growth were as follows:

	Three Months Ended March 31,			
$ in Millions	2012	2011	$ Change	Points Attribution
Total NWP	$8,078	$7,583	$495	6.5
Components of Growth:				
International local businesses (excluding foreign exchange)	1,378	1,191	187	2.5
Domestic personal auto	1,980	1,836	144	1.9
-Domestic homeowners	920	815	105	1.4
-Homeowners quota share	(163)	(145)	(18)	(0.2)
Total Homeowners	757	670	87	1.2
Lloyd's Syndicate 4472	560	515	45	0.6
Individual life	85	69	16	0.2
Group disability and life	196	207	(11)	(0.1)
Surety	172	189	(17)	(0.2)
Foreign exchange	(45)	-	(45)	(0.6)
Other commercial lines	2,995	2,906	89	1.0
Total NWP	$8,078	$7,583	$495	6.5

Consolidated NWP by geographic distribution channels was as follows:

	Three Months Ended March 31,		
$ in Millions	2012	2011	Change
U.S.	$6,096	$5,809	4.9%
International[1]	1,982	1,774	11.7
Total NWP	$8,078	$7,583	6.5%

1 Excludes domestically written business in the International SBU.

NWP for the three months ended March 31, 2012 was $8.078 billion, an increase of $495 million over the same period in 2011. Significant changes by major line of business include:

- Private passenger automobile NWP increased $218 million over the same period in 2011. The increase primarily reflects growth of policies in-force and rate increases in Personal Markets and LMAC, organic growth in International's local businesses, primarily in Latin America, and the acquisition of Quinn Insurance Limited ("QIL") in Ireland in November 2011.
- Workers compensation NWP decreased $52 million from the same period in 2011. The decrease primarily reflects a construction account with multi-year exposures written in 2011 in Commercial Markets that did not recur, and a decline in new business premium due to disciplined underwriting in a continued competitive market, partially offset by rate increases, favorable audit premium and the workers compensation "booked as billed" adjustment in Corporate and Other.
- Homeowners NWP increased $87 million over the same period in 2011. The increase primarily reflects growth of policies in-force and rate increases in Personal Markets and LMAC.
- International local businesses NWP (excluding private passenger automobile) increased $78 million over the same period in 2011. The increase was primarily driven by organic growth in Latin America led by Venezuela (primarily due to inflation) and, to a lesser extent, Asia led by China and the acquisition of QIL.

- Lloyd's Syndicate 4472 NWP increased $45 million over the same period in 2011. The increase was largely due to favorable rates in certain lines of business.
- LIU third party NWP increased $53 million over the same period in 2011. The increase primarily reflects new business from casualty and specialty casualty lines.
- Surety NWP decreased $17 million from the same period in 2011. The decrease was primarily due to a reduction in the number of contract bonds issued and lower average bond size.
- Individual life NWP increased $16 million over the same period in 2011. The increase was primarily driven by strong structured settlement sales in 2012 compared to 2011.

More detailed explanations of the changes in NWP by line of business are included in the related discussion of financial results for each segment.

For a more complete 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.

Results of Operations – Consolidated

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Revenues	$8,881	$8,381	6.0%
PTOI before catastrophes, net incurred losses attributable to prior years and LP and LLC income	$793	$616	28.7%
Catastrophes[1]	(321)	(588)	(45.4)
Net incurred losses attributable to prior years:			
- Asbestos & environmental	(2)	(1)	100.0
- All other[2]	(14)	210	NM
PTOI before LP and LLC income	456	237	92.4
LP and LLC income[3]	121	210	(42.4)
PTOI	577	447	29.1
Net realized gains	49	76	(35.5)
Loss on extinguishment of debt	(15)	-	NM
Pre-tax income	611	523	16.8
Income tax expense	(155)	(156)	(0.6)
Consolidated net income	456	367	24.3
Less: Net (loss) income attributable to non-controlling interest	(3)	3	NM
Net income attributable to LMHC	$459	$364	26.1%
Cash flow from operations	$651	$622	4.7%

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of $14 million and $7 million for the three months ended March 31, 2012 and 2011, respectively. Net of amortization of deferred gains on retroactive reinsurance of $11 million and $99 million for the three months ended March 31, 2012 and 2011, respectively. 2011 reflects a gain on commutation of two retroactive reinsurance contracts during the first quarter.

3 LP and LLC income is included in net investment income in the consolidated statements of income.

NM = Not Meaningful

PTOI for the three months ended March 31, 2012 was $577 million, an increase of $130 million over the same period in 2011. The increase was primarily driven by premium growth, better non-catastrophe property experience and lower catastrophe losses (primarily International), partially offset by lower LP and LLC income and unfavorable net incurred losses attributable to prior years compared to favorable development in 2011 (including a gain on the commutation of two retroactive reinsurance contracts.)

Revenues for the three months ended March 31, 2012 were $8.881 billion, an increase of $500 million over the same period in 2011. The major components of revenues are net premium earned, net investment income, net realized gains, and fee and other revenues.

Net premium earned for the three months ended March 31, 2012 was $7.727 billion, an increase of $546 million over the same period in 2011. The increase primarily reflects personal lines increases due to rate increases and growth in policies in-force in Personal Markets and LMAC, as well as organic growth in International, primarily Latin America, and the acquisition of QIL partially offset by the impact of foreign exchange.

Net investment income for the three months ended March 31, 2012 was $862 million, a decrease of $53 million from the same period in 2011. The change in the period primarily reflects valuation changes in LP and LLC investments partially offset by increases in taxable interest income due to a higher invested asset

base as a result of the acquisition of the Ireland operations and continued reinvestment of cash flow from operations.

Net realized gains for the three months ended March 31, 2012 were $49 million, a decrease of $27 million from the same period in 2011. The decrease was primarily related to higher other-than-temporary impairments and lower gains in 2012 on common equities as well as gains associated with fair value option elections recognized in 2011 that did not recur in 2012. The decrease was partially offset by gains recognized in connection with the sale of fixed maturity securities.

Fee and other revenues for the three months ended March 31, 2012 were $243 million, an increase of $34 million over the same period in 2011. The increase primarily reflects higher oil and gas revenues in Corporate and Other due to increased production.

Claims, benefits and expenses for the three months ended March 31, 2012 were $8.255 billion, an increase of $397 million over the same period in 2011. The increase was driven by unfavorable incurred losses attributable to prior years compared to favorable incurred losses attributable to prior years in 2011, a gain on the commutation of two workers compensation retroactive reinsurance agreements that occurred in 2011 and an increase in losses and expenses consistent with business growth, partially offset by lower catastrophe losses.

Income tax expense for the three months ended March 31, 2012 was $155 million, a decrease of $1 million from the same period in 2011. The Company's effective tax rate for the three months ended March 31, 2012 was 25% compared to 30% for the same period in 2011. The primary driver of the decrease in the effective tax rate from 2011 to 2012 was due to a tax expense in the first quarter of 2011 and a tax benefit in the first quarter of 2012 for revisions to prior year estimates. The Company's effective tax rate differs from the Federal statutory rate of 35% principally due to tax-exempt investment income.

Net income attributable to LMHC for the three months ended March 31, 2012, was $459 million, an increase of $95 million over the same period in 2011.

Cash flow from operations for the three months ended March 31, 2012 was $651 million, an increase of $29 million over the same period in 2011. The increase was primarily driven by higher premium collections and a federal income tax refund, partially offset by the impact of QIL cash outflow and higher paid losses and expenses consistent with business growth.

	Three Months Ended March 31,		
	2012	2011	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	66.7%	68.2%	(1.5%)
Underwriting expense ratio	29.2	28.5	0.7
Dividend ratio	0.1	0.2	(0.1)
Subtotal	96.0	96.9	(0.9)
Catastrophes[1]	4.4	8.6	(4.2)
Net incurred losses attributable to prior years:			
- Asbestos & environmental	0.4	-	0.4
- All other	0.1	(3.1)	3.2
Total combined ratio[2]	100.9%	102.4%	(1.5)

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 The combined 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 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 managed care income) 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 unless related to an asbestos and environmental commutation.

The consolidated combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2012 was 96.0%, a decrease of 0.9 points from the same period in 2011. The decrease in the claims and claim adjustment expense ratio reflects lower commercial lines property and homeowners losses and favorable auto physical damage frequency loss trends in Personal Markets. The increase in the underwriting expense ratio reflects increased advertising and information technology expenditures (Personal Markets and LMAC) and higher underwriting expenses in International (due to the addition of Ireland).

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2012 was 100.9%, a decrease of 1.5 points from the same period in 2011. The decrease reflects the changes in the combined ratio previously discussed as well as lower catastrophe losses (primarily International), partially offset by unfavorable net incurred losses attributable to prior years in 2012 versus favorable net incurred losses attributable to prior years in 2011 (including a gain on the commutation of two retroactive reinsurance contracts.)

LIBERTY MUTUAL AGENCY CORPORATION

Overview – Liberty Mutual Agency Corporation

LMAC sells personal and commercial insurance products and services to individuals and small to mid-sized businesses through independent agents throughout the United States. Commercial lines products are offered through eight regional insurance companies that combine local underwriting, market knowledge and service orientation with the scale advantages of a national company. Personal lines products are distributed nationally under the Safeco brand, with an emphasis on service, and product and pricing sophistication. Liberty Mutual Surety is a leading provider of nationwide contract and commercial surety bonds to businesses of all sizes.

LMAC NWP by segment was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Personal	$1,304	$1,201	8.6%
Commercial	1,074	1,079	(0.5)
Surety	172	187	(8.0)
Corporate and Other[1]	26	36	(27.8)
Total NWP	$2,576	$2,503	2.9%

1 Includes run-off operations and internal reinsurance.

LMAC NWP by line of business was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Commercial Lines			
Commercial multiple peril	$456	$448	1.8%
Commercial automobile	246	257	(4.3)
Workers compensation	209	219	(4.6)
Surety	172	189	(9.0)
General liability	114	115	(0.9)
Other	70	70	-
Subtotal	$1,267	$1,298	(2.4)
Personal Lines			
Private passenger automobile	$799	$749	6.7
Homeowners	392	349	12.3
Other	118	107	10.3
Subtotal	$1,309	$1,205	8.6
Total NWP	$2,576	$2,503	2.9%

NWP for the three months ended March 31, 2012 was $2.576 billion, an increase of $73 million over the same period in 2011.

Commercial lines NWP for the three months ended March 31, 2012 was $1.267 billion, a decrease of $31 million from the same period in 2011. The decrease reflects a decline in new business premium due to disciplined underwriting in a continued competitive marketplace and lower average policy size (primarily due to line of business mix change), partially offset by rate increases and favorable audit premiums. The period was further impacted by a decline in Surety premium largely due to a reduction in the number of contract bonds issued and lower average bond size.

Personal lines NWP for the three months ended March 31, 2012 was $1.309 billion, an increase of $104 million over the same period in 2011. The increase reflects policies in-force growth of 5.3% across all product lines primarily due to strong new business. The period was further impacted by higher rates and increased auto average written premium due to a continued shift to annual private passenger auto policies.

Results of Operations – Liberty Mutual Agency Corporation

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Revenues	$2,858	$2,812	1.6%
PTOI before catastrophes, net incurred losses attributable to prior years and LP and LLC income	$361	$314	15.0
Catastrophes[1]	(188)	(195)	(3.6)
Net incurred losses attributable to prior years[2]	17	98	(82.7)
PTOI before LP and LLC income	190	217	(12.4)
LP and LLC income[3]	1	-	NM
PTOI	$191	$217	(12.0%)

1 Catastrophes include all current and prior accident year catastrophe losses incurred. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.
2 Net of earned premium attributable to prior years of zero for the three months ended March 31, 2012 and 2011, respectively.
3 LP and LLC income is included in net investment income in the consolidated statements of income.
NM = Not Meaningful

PTOI for the three months ended March 31, 2012 was $191 million, a decrease of $26 million from the same period in 2011. The decrease was driven by lower favorable net incurred losses attributable to prior years primarily due to increased Surety claims activity, higher commercial lines liability losses, and higher expenses primarily due to increased advertising and technology expenditures. These items were partially offset by lower non-catastrophe losses on the commercial lines property and homeowners lines of business, consistent with mild weather, growth in net premium earned, and lower catastrophe losses (partially due to reduction in prior period catastrophe losses).

Revenues for the three months ended March 31, 2012 were $2.858 billion, an increase of $46 million over the same period in 2011. The major components of revenues are net premium earned, net investment income, and net realized gains.

Net premium earned for the three months ended March 31, 2012 was $2.632 billion, an increase of $78 million over the same period in 2011. The increase reflects increased personal lines rate and new business, as well as favorable commercial lines audit premiums.

Net investment income for the three months ended March 31, 2012 was $197 million, a decrease of $7 million from the same period in 2011. The decrease was primarily driven by lower investment yields.

Net realized gains for the three months ended March 31, 2012 were $5 million, a decrease of $25 million from the same period in 2011. The decrease was primarily driven by the higher impairments taken in 2012 on common equities and due to a gain on sale of business segment in 2011 that did not recur in 2012.

Claims, benefits and expenses for the three months ended March 31, 2012 were $2.662 billion, an increase of $97 million over the same period in 2011. The increase was driven by lower favorable net incurred losses attributable to prior years, primarily due to increased surety claims activity, higher commercial lines liability losses, and higher expenses primarily due to increased advertising and technology expenditures, partially offset by lower non-catastrophe losses on the commercial lines property and homeowners lines of business, consistent with mild weather, and lower catastrophe losses (partially due to reduction in prior period catastrophe losses).

	Three Months Ended March 31,		
	2012	**2011**	**Change (Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	60.7%	62.7%	(2.0)
Underwriting expense ratio	31.6	31.4	0.2
Dividend ratio	0.2	0.2	-
Subtotal	92.5	94.3	(1.8)
Catastrophes[1]	7.1	7.7	(0.6)
Net incurred losses attributable to prior years	(0.7)	(3.8)	3.1
Total combined ratio	98.9%	98.2%	0.7

1 Catastrophes include all current and prior accident year catastrophe losses incurred. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

The LMAC combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2012 was 92.5%, a decrease of 1.8 points from the same period in 2011. The decrease in the claims and claim adjustment expense ratio reflects decreased losses on the commercial lines property and homeowners lines of business, consistent with mild weather, partially offset by higher commercial lines liability losses. The increase in the underwriting expense ratio reflects increased advertising and technology expenditures.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2012 was 98.9%, an increase of 0.7 points over the same period in 2011. The increase was primarily driven by less favorable net incurred losses attributable to prior years, primarily due to increased surety claims activity, partially offset by lower catastrophe losses (partially due to reduction in prior period catastrophe losses).

INTERNATIONAL

Overview – International

International sells insurance products and services through two distinct approaches: local businesses, which sell personal and small commercial lines products, and LIU which sells specialty commercial insurance and reinsurance worldwide. International's local business operations consist of local insurance operations selling property, casualty, health and life insurance products to individuals and businesses in three geographic regions: Latin America, including Venezuela, Brazil, Colombia, Argentina and Chile; Europe, including Spain, Portugal, Turkey, Poland, Ireland (as a result of the QIL acquisition in November 2011) and Russia (as a result of the KIT Finance Insurance acquisition in March 2012); and Asia, including Thailand, Singapore, China (including Hong Kong) and Vietnam. Private passenger automobile insurance is the single largest line of business. LIU writes casualty, specialty casualty, marine, energy, construction, aviation, property, crisis management and trade credit coverage and other specialty programs through offices in Asia, Australia, Europe, the Middle East, North America and Latin America. LIU, through its Lloyd's Syndicate 4472, also provides multi-line insurance and reinsurance worldwide.

International NWP by market segment was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
International Local Businesses Total	$1,318	$1,174	12.3%
- Latin America	892	803	11.1
- Europe	323	279	15.8
- Asia	103	92	12.0
LIU	911	816	11.6
Total NWP	$2,229	$1,990	12.0%
Foreign exchange effect on growth			(2.3%)
NWP growth excluding foreign exchange			14.3%

International’s major product lines are as follows:

(1) Local businesses: personal, primarily private passenger automobile, and commercial insurance;
(2) Lloyd’s Syndicate 4472: multi-line insurance and reinsurance with an emphasis on property, contingent lines, marine reinsurance and property and casualty reinsurance;
(3) LIU inland marine program: handset protection coverage for lost or damaged devices;
(4) LIU third party: includes casualty, excess casualty, directors and officers, errors and omissions, environmental impairment liability, commercial automobile, railroad and other;
(5) LIU first party: includes marine, energy, construction, aviation and property; and
(6) LIU other: includes workers compensation, surety, trade credit, E&S property and crisis management.

International NWP by line of business was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Local businesses – private passenger auto	$745	$672	10.9%
Local businesses – all other[1]	573	502	14.1
Lloyd's Syndicate 4472	501	454	10.4
LIU third party	223	184	21.2
LIU inland marine program	108	96	12.5
LIU first party	58	68	(14.7)
LIU other	21	14	50.0
Total NWP	$2,229	$1,990	12.0%

1 Premium related to other personal lines and commercial insurance products sold by local business operations.

NWP for the three months ended March 31, 2012 was $2.229 billion, an increase of $239 million over the same period in 2011. The increase reflects organic growth in local operations, primarily Latin America, led by Venezuela (primarily due to the impact of inflation) and Brazil, and to a lesser extent, Asia, led by China. The increase also reflects the addition of Ireland. LIU also contributed to the increase, primarily driven by Lloyd's Syndicate 4472 business largely due to favorable rates in certain lines of business, and to a lesser extent, LIU third party, due to new business from casualty and specialty casualty lines. The increase was partially offset by foreign exchange impact (approximately $46 million).

Results of Operations – International

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Revenues	$2,267	$1,973	14.9%
PTOI before catastrophes and net incurred losses attributable to prior years	$187	$154	21.4%
Catastrophes[1]	7	(252)	NM
Net incurred losses attributable to prior years[2]	(44)	39	NM
Pre-tax operating income (loss)	$150	($59)	NM

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines (reinsurance assumed through Lloyd's Syndicate 4472) except for the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of ($1) million and $7 million for the three months ended March 31, 2012 and 2011, respectively

NM = Not Meaningful

PTOI for the three months ended March 31, 2012 was $150 million, versus a pre-tax operating loss of $59 million in the same period in 2011. The increase was primarily driven by the absence of catastrophe losses in 2012 compared to the catastrophe losses related to the Australia floods, Cyclone Yasi, Japan earthquake and tsunami and New Zealand earthquakes in 2011. The increase was partially offset by unfavorable net incurred losses attributable to prior years, compared to favorable net incurred losses attributable to prior years in 2011 (primarily within Lloyd's Syndicate 4472 business in both years). Foreign exchange also contributed to the increase slightly (approximately $6 million).

Revenues for the three months ended March 31, 2012 were $2.267 billion, an increase of $294 million over the same period in 2011. The primary components of revenues are net premium earned and net investment income.

Net premium earned for the three months ended March 31, 2012 was $2.036 billion, an increase of $250 million over the same period in 2011. The increase reflects the previously mentioned growth in NWP in 2012 and the last quarter of 2011.

Net investment income for the three months ended March 31, 2012 was $178 million, an increase of $31 million over the same period in 2011. The increase reflects a higher invested asset base due to the reinvestment of cash flow from operations driven by the growth in NWP, the addition of Ireland and higher yields in local operations, primarily in Latin America led by Argentina, as well as Lloyd's Syndicate 4472.

Claims, benefits and expenses for the three months ended March 31, 2012 was $2.104 billion, an increase of $78 million over the same period in 2011. The increase reflects higher current accident year claims and claim adjustment expenses primarily driven by the organic growth in Latin America, the addition of Ireland, as well as unfavorable incurred losses attributable to prior years, compared to favorable incurred losses attributable to prior years in 2011 (primarily within Lloyd's Syndicate 4472 business). The increase was partially offset by the absence of catastrophe losses in 2012 compared to the catastrophe losses related to the Australia floods, Cyclone Yasi, Japan earthquake and tsunami and New Zealand earthquakes in 2011.

	Three Months Ended March 31,		
	2012	**2011**	**Change (Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	67.2%	66.7%	0.5
Underwriting expense ratio	31.8	31.5	0.3
Dividend ratio	-	-	-
Subtotal	99.0	98.2	0.8
Catastrophes[1]	(0.4)	14.3	(14.7)
Net incurred losses attributable to prior years	2.3	(2.2)	4.5
Total combined ratio	100.9%	110.3%	(9.4)

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines (reinsurance assumed through Lloyd's Syndicate 4472) except for the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

The International combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2012 was 99.0%, an increase of 0.8 points over the same period in 2011. The increase reflects higher non-catastrophe claims and claim adjustment expenses and underwriting expenses, primarily driven by the addition of Ireland in 2012.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2012 was 100.9%, a decrease of 9.4 points from the same period in 2011. The decrease reflects the absence of catastrophe losses in 2012 compared to the catastrophe losses related to the Australia floods, Cyclone Yasi, Japan earthquake and tsunami and New Zealand earthquakes in 2011, partially offset by unfavorable net incurred losses attributable to prior years, compared to favorable net incurred losses attributable to prior years in 2011 (primarily within Lloyd's Syndicate 4472 business) and the changes in the combined ratio previously discussed.

PERSONAL MARKETS

Overview – Personal Markets

Personal Markets sells automobile, homeowners and other types of property and casualty insurance coverage, as well as a wide range of life and annuity products, to individuals in the United States. Products are distributed through more than 2,200 licensed captive sales representatives, approximately 500 licensed telesales counselors, third-party producers (including banks for life products) and the Internet. Personal Markets' largest source of new business is through its 13,500 sponsored affinity groups (including employers, professional and alumni associations, credit unions, and other partnerships).

Personal Markets NWP by line of business was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Private passenger automobile	$1,180	$1,085	8.8%
Homeowners and other	585	523	11.9
Individual life	81	67	20.9
Total NWP	$1,846	$1,675	10.2%

NWP for the three months ended March 31, 2012 was $1.846 billion, an increase of $171 million over the same period in 2011.

Private passenger automobile NWP for the three months ended March 31, 2012 was $1.180 billion, an increase of $95 million over the same period in 2011. The increase reflects 3.6% growth in policies in-force as compared to March 31, 2011 as well as rate increases.

Homeowners and other NWP for the three months ended March 31, 2012 was $585 million, an increase of $62 million over the same period in 2011. The increase reflects 5.0% growth in homeowners policies in-force as compared to March 31, 2011 as well as rate increases.

Individual life NWP for the three months ended March 31, 2012 was $81 million, an increase of $14 million over the same period in 2011. The increase was driven by strong structured settlement sales in 2012 compared to 2011.

Results of Operations – Personal Markets

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Revenues	$2,081	$1,917	8.6%
PTOI before catastrophes and net incurred losses attributable to prior years	$345	$282	22.3
Catastrophes[1]	(116)	(121)	(4.1)
Net incurred losses attributable to prior years	(10)	5	NM
PTOI	$219	$166	31.9%

1 Catastrophes include all current and prior accident year catastrophe losses incurred. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

NM = Not Meaningful

PTOI for the three months ended March 31, 2012 was $219 million, an increase of $53 million over the same period in 2011. The increase was primarily driven by favorable non-catastrophe underwriting results as well as the impact of growth in net premium earned versus the prior year.

Revenues for the three months ended March 31, 2012 were $2.081 billion, an increase of $164 million over the same period in 2011. The major components of revenues are net premium earned and net investment income.

Net premium earned for the three months ended March 31, 2012 was $1.841 billion, an increase of $151 million over the same period in 2011. The increase reflects the premium earned associated with the changes in NWP previously discussed and NWP growth in 2011.

Net investment income for the three months ended March 31, 2012 was $200 million, an increase of $9 million over the same period in 2011. The increase was driven by a higher invested asset base compared to the prior year.

Claims, benefits and expenses for the three months ended March 31, 2012 were $1.861 billion, an increase of $113 million over the same period in 2011. The increase primarily reflects an increase in losses and expenses consistent with business growth.

	Three Months Ended March 31,		
			Change
	2012	2011	(Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	61.5%	63.6%	(2.1)
Underwriting expense ratio	24.6	24.2	0.4
Dividend ratio	-	-	-
Subtotal	86.1	87.8	(1.7)
Catastrophes[1]	6.6	7.5	(0.9)
Net incurred losses attributable to prior years	0.5	(0.4)	0.9
Total combined ratio	93.2%	94.9%	(1.7)

1 Catastrophes include all current and prior accident year catastrophe losses incurred. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

The Personal Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2012 was 86.1%, a decrease of 1.7 points from the same period in 2011. The decrease in the claims and claim adjustment expense ratio primarily reflects favorable non-catastrophe results in the homeowners and auto physical damage lines of business. The underwriting expense ratio increased 0.4 points over 2011 as a result of an investment in growth-related items, primarily increased captive sales representatives, and higher advertising and information technology expenditures.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2012 was 93.2%, a decrease of 1.7 points from the same period in 2011. This reflects the changes in the combined ratio previously discussed. Additionally, lower catastrophe losses were completely offset by unfavorable net incurred losses attributable to prior years in 2012 versus favorable net incurred losses attributable to prior years in 2011.

COMMERCIAL MARKETS

Overview – Commercial Markets

Commercial Markets sells a wide array of property and casualty and group benefits insurance coverages through independent agents, brokers and benefit consultants throughout the United States. Commercial Markets P&C provides commercial lines products and services to mid-sized and large businesses (with an annual cost of risk of $150,000 or more). Group Benefits provides midsized and large businesses with short- and long-term disability insurance products and administrative services and group life insurance through Liberty Life Assurance Company of Boston, a subsidiary of the Company. Summit provides workers compensation in the Southeast (mainly Florida) primarily to small businesses. Liberty Mutual Reinsurance provides reinsurance programs to domestic and foreign insurance and reinsurance companies. The Company is also a servicing carrier for state based workers compensation involuntary market pools.

Commercial Markets NWP by market segment was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Commercial Markets P&C	$1,070	$1,159	(7.7%)
Group Benefits	196	207	(5.3)
Summit	188	166	13.3
Liberty Mutual Reinsurance	91	57	59.6
Total NWP	$1,545	$1,589	(2.8%)

Commercial Markets NWP by line of business was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Workers compensation	$865	$944	(8.4%)
Group disability and life	196	207	(5.3)
General liability	154	169	(8.9)
Commercial multiple peril / fire	124	107	15.9
Commercial automobile	115	93	23.7
Other (including AVR)	91	69	31.9
Total NWP	$1,545	$1,589	(2.8%)

NWP for the three months ended March 31, 2012 was $1.545 billion, a decrease of $44 million from the same period in 2011. The decrease reflects two large transactions from 2011 that did not recur - a construction account with multi-year exposures in the workers compensation and general liability lines of business in the Commercial Markets P&C segment and a large disability account written in Group Benefits. The decrease was partially offset by increased rate and exposures across all property and casualty lines of business, most notably in workers compensation. The period also reflects an increase in commercial auto premium related to retrospectively rated contracts, increased new business writings in Commercial Markets P&C's general liability and property lines of business, and an increase in NWP in Liberty Mutual Reinsurance due to a change in an assumed program structure.

Result s of Operations – Commercial Markets

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Revenues	$1,614	$1,559	3.5%
PTOI before catastrophes and net incurred losses attributable to prior years	$113	$83	36.1%
Catastrophes[1]	(53)	(50)	6.0
Net incurred losses attributable to prior years[2]	9	(3)	NM
PTOI	$69	$30	130.0%

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's assumed voluntary reinsurance except for the 2011 Australia floods, Japan earthquake and tsunami, New Zealand earthquakes, and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of $15 million and zero for the three months ended March 31, 2012 and 2011, respectively. Net of amortization of deferred gains on assumed retroactive reinsurance of $1 million and zero for the three months ended March 31, 2012 and 2011, respectively.

NM = Not Meaningful

PTOI for the three months ended March 31, 2012 was $69 million, an increase of $39 million over the same period in 2011. The increase reflects an increase in Group Benefits' earnings driven by an improvement in long-term disability losses and growth in the property book of business combined with improved non-catastrophe loss experience. The increase also reflects favorable prior accident year development related to assumed involuntary market pools.

Revenues for the three months ended March 31, 2012 were $1.614 billion, an increase of $55 million over the same period in 2011. The major components of revenues are net premium earned, net investment income and fee and other revenues.

Net premium earned for the three months ended March 31, 2012 was $1.326 billion, an increase of $50 million over the same period in 2011. The increase reflects higher rates across all property and casualty lines of business, and growth in property and Liberty Mutual Reinsurance. The increase also reflects favorable premium development on prior accident year exposures in the assumed involuntary market pools. The increase was partially offset by the large disability account written in Group Benefits from 2011 that did not recur.

Net investment income for the three months ended March 31, 2012 was $217 million, representing no change from the same period in 2011.

Fee and other revenues for the three months ended March 31, 2012 were $71 million, an increase of $5 million over the same period in 2011. The increase reflects higher commission revenues from the Company's servicing carrier operations due to higher involuntary market premium volume. As a servicing carrier, the Company receives fee income for performing certain underwriting, claims and administrative services for all participating involuntary pool members.

Claims, benefits, and expenses for the three months ended March 31, 2012 were $1.545 billion, an increase of $16 million over the same period in 2011. The increase was attributable to business growth and a higher commission expense reflecting a modest shift in premium away from the workers compensation line of business to lines of business with higher commission structures. The increase was partially offset by costs associated with a large disability account written in 2011 that did not recur.

	Three Months Ended March 31,		
	2012	2011	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	84.1%	85.6%	(1.5)
Underwriting expense ratio	24.4	24.6	(0.2)
Dividend ratio	0.5	0.7	(0.2)
Subtotal	109.0	110.9	(1.9)
Catastrophes[1]	4.8	4.7	0.1
Net incurred losses attributable to prior years	(1.0)	0.3	(1.3)
Total combined ratio	112.8%	115.9 %	(3.1)

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's assumed voluntary reinsurance except for the 2011 Australia floods, Japan earthquake and tsunami, New Zealand earthquakes, and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

The Commercial Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2012 was 109.0%, a decrease of 1.9 points from the same period in 2011. The decrease in the claims and claim adjustment expense ratio reflects lower current accident year non-catastrophe property-related losses and a modest shift in business mix away from the workers compensation line of business.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2012 was 112.8%, a decrease of 3.1 points from the same period in 2011. The decrease reflects the changes in the combined ratio previously discussed as well as favorable development of assumed involuntary net incurred losses attributable to prior years.

CORPORATE AND OTHER

Overview – Corporate and Other

Corporate and Other includes the following significant items:

- Certain internal discontinued operations composed of: asbestos, environmental, and toxic tort exposures, the run-off of certain LMAC business, the run-off of the California workers compensation business of Golden Eagle Insurance Corporation, certain distribution channels related to Prudential Property and Casualty Insurance Company, Prudential General Insurance Company and Prudential Commercial Insurance Company (together, "PruPac").

- Effective July 1, 2011, Corporate and Commercial Markets novated their reinsurance treaty that applied to certain pre-2005 workers compensation claims and entered into two new agreements including: (1) certain pre-2011 voluntary workers compensation claims and, (2) certain pre-2011 involuntary workers compensation claims.

- Interest expense on the Company's outstanding debt.

- Certain risks of its SBUs that the Company reinsures as part of its risk management program, and risks on Personal Markets homeowners business covered by the externally ceded homeowners quota share reinsurance treaty.

- The Company reports its written premium on workers compensation contracts on the "booked as billed" method. Commercial Markets reports workers compensation written premium on the "booked at inception" method. Corporate and Other results reflect the difference between these two methods.

- The Company discounts the long-term indemnity portion of its settled unpaid workers compensation claims at risk-free discount rates. Commercial Markets reports its discount based on statutory discount rates. Corporate and Other results reflect the difference between the statutory and risk-free rate.

- Costs associated with certain long-term compensation plans and other corporate costs not allocated to the SBUs.

- For presentation in this MD&A, excluding LMAC, domestic property and casualty operations' investment income is allocated to the business units based on planned ordinary investment income returns by investment category. Investments are allocated to the business units in an amount equal to their respective liabilities net of insurance assets (reinsurance, premiums receivable, etc.) plus allocated statutory policyholders' surplus. The difference between allocated net investment income and actual net investment income is included in Corporate and Other.

- Income related to LP and LLC investments, excluding LMAC activity.

- Fee and other revenues include revenues from the Company's wholly owned subsidiary, Liberty Energy, and lease and other income on investment properties. Liberty Energy generates revenue from the production and sale of oil and gas.

- Effective January 1, 2011, certain retroactive reinsurance agreements previously reported within Commercial Markets.

Corporate and Other NWP by line of business was as follows:

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Reinsurance, net	($44)	($60)	(26.7%)
Workers compensation[1]	(74)	(114)	(35.1)
Total NWP	($118)	($174)	(32.2%)

[1] Booked as billed adjustment.

NWP for the three months ended March 31, 2012 was ($118) million, an increase of $56 million over the same period in 2011. The change was primarily due to an increase in the Company's workers compensation "booked as billed" adjustment primarily related to a large contract in 2011 that did not recur and an increase in assumed premium related to the Company's internal reinsurance program, partially offset by an increase in ceded premium related to the Personal Markets homeowners quota share treaty.

Results of Operations – Corporate and Other

	Three Months Ended March 31,		
$ in Millions	**2012**	**2011**	**Change**
Revenues	$61	$120	(49.2%)
Pre-tax operating (loss) income before catastrophes, net incurred losses attributable to prior years and LP and LLC income	($213)	($217)	(1.8%)
Catastrophes[1]	29	30	(3.3)
Net incurred losses attributable to prior years:			
- Asbestos & environmental	(2)	(1)	100.0
- All other[2]	14	71	(80.3)
Pre-tax operating loss before LP and LLC income	(172)	(117)	47.0
LP and LLC income [3]	120	210	(42.9)
Pre-tax operating (loss) income	($52)	$93	NM

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods and the tornadoes and other severe storms in the U.S. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums of zero for the three months ended March 31, 2012 and 2011, respectively.

2 Net of earned premium attributable to prior years of zero for the three months ended March 31, 2012 and 2011, respectively. Net of amortization of deferred gains on retroactive reinsurance of $10 million and $99 million for the three months ended March 31, 2012 and 2011, respectively. 2011 reflects a gain on commutation of two retroactive reinsurance contracts during the first quarter.

3 LP and LLC income is included in net investment income in the consolidated statements of income.

NM = Not Meaningful

Pre-tax operating loss for the three months ended March 31, 2012 was $52 million, versus PTOI of $93 million in the same period in 2011. The decrease was primarily driven by valuation changes in LP and LLC investments and a gain on the commutation of two workers compensation retroactive reinsurance agreements that occurred in 2011, partially offset by a decrease in the amount of incurred losses attributable to prior years related to pre-2011 workers compensation business assumed from Commercial Markets and a decrease in interest expense as a result of debt repurchases in 2011.

Revenues for the three months ended March 31, 2012 were $61 million, a decrease of $59 million from the same period in 2011. The major components of revenues are net premium earned, net investment income, net realized gains, and fee and other revenues.

Net premium earned for the three months ended March 31, 2012 was ($108) million, an increase of $17 million over the same period in 2011. The increase reflects the earned premium associated with the changes in reinsurance NWP previously discussed.

Net investment income for the three months ended March 31, 2012 was $70 million, a decrease of $86 million from the same period in 2011. The decrease primarily reflects valuation changes in LP and LLC investments.

Net realized gains for the three months ended March 31, 2012 were $30 million, a decrease of $7 million from the same period in 2011. The decrease was primarily related to higher other-than-temporary impairments and lower gains in 2012 on common equities as well as gains associated with fair value option elections recognized in 2011 that did not recur in 2012. The decrease was partially offset by gains recognized in connection with the sale of fixed maturity securities.

Fee and other revenues for the three months ended March 31, 2012 were $69 million, an increase of $17 million over the same period in 2011. The increase primarily reflects higher oil and gas revenues due to increased production.

Claims, benefits and expenses for the three months ended March 31, 2012 were $83 million, an increase of $93 million over the same period in 2011. The increase was due to the commutation of two workers compensation retroactive reinsurance agreements that occurred in 2011, an increase in internally assumed losses related to reinsurance programs, and higher depreciation charges related to Liberty Energy, partially offset by a decrease in the amount of incurred losses attributable to prior years related to pre-2011 workers compensation business assumed from Commercial Markets and a decrease in interest expense as a result of debt repurchases in 2011.

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. A relatively safe and stable income stream is achieved by maintaining a broadly based portfolio of investment grade bonds. These 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 commercial mortgages and other real estate financing investments, non-investment grade bonds, including syndicated bank loans, common and preferred stock, private equity and direct investments in natural resource 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 predominantly uses a subsidiary investment adviser registered with the Securities and Exchange Commission for managing and administering the investment portfolios of its domestic and foreign insurance operations.

Invested Assets (including cash and cash equivalents)

The following table summarizes the Company's invested assets by asset category as of March 31, 2012 and December 31, 2011:

$ in Millions	**As of March 31, 2012**		**As of December 31, 2011**	
Invested Assets by Type	**Carrying Value**	**% of Total**	**Carrying Value**	**% of Total**
Fixed maturities, available for sale, at fair value	$62,502	82.4%	$60,576	82.2%
Equity securities, available for sale, at fair value	2,281	3.0	1,954	2.7
LPs and LLCs	3,738	4.9	3,389	4.6
Commercial mortgage loans	1,197	1.6	1,196	1.6
Short-term investments	273	0.4	201	0.3
Other investments	473	0.6	400	0.5
Cash and cash equivalents	5,410	7.1	5,972	8.1
Total invested assets	$75,874	100.0%	$73,688	100.0%

Total invested assets as of March 31, 2012 were $75.874 billion, an increase of $2.186 billion or 3.0% over December 31, 2011. The increase reflects an increase in unrealized gains related to tightening credit spreads, positive equity market performance, and the reinvestment of cash flow from operations.

Fixed maturities as of March 31, 2012 were $62.502 billion, an increase of $1.926 billion or 3.2% over December 31, 2011. The increase reflects investment of cash associated with the QIL acquisition, an increase in unrealized gains related to tightening credit spreads, and the reinvestment of cash flow from operations. As of March 31, 2012, the Company had commitments to purchase various residential mortgage-backed securities at a cost and fair value of $103 million and various corporate and municipal securities at a cost and fair value of $99 million.

Equity securities available for sale as of March 31, 2012 were $2.281 billion ($1.886 billion common stock and $395 million preferred stock) versus $1.954 billion as of December 31, 2011 ($1.608 billion common

stock and $346 million preferred stock), an increase of $327 million or 16.7% over December 31, 2011. Of the $1.886 billion of common stock at March 31, 2012, $298 million relates to securities associated with non-guaranteed unit linked products where the policyholder bears the investment risk. The increase in total equity securities available for sale was consistent with the Company's continued investment in this asset class as well as broader equity market performance.

Investments in LPs and LLCs as of March 31, 2012 were $3.738 billion, an increase of $349 million or 10.3% over December 31, 2011. These investments consist of traditional private equity partnerships of $2.075 billion, other partnerships (primarily energy) of $1.061 billion, and real estate partnerships of $602 million. The increase reflects improved equity valuations and new investments. The Company's investments in LPs and LLCs are long-term in nature and highly illiquid. The Company believes these investments offer the potential for superior long-term returns and are appropriate in the overall context of a diversified portfolio.

As of March 31, 2012, the Company had unfunded commitments in traditional private equity partnerships, real estate, energy, and other of $896 million, $466 million, $871 million, and $418 million, respectively.

Commercial mortgage loans as of March 31, 2012 were $1.197 billion (net of $17 million of loan loss reserves or 1.4% of the outstanding loan portfolio), an increase of $1 million or 0.1% over December 31, 2011. The increase primarily reflects a $19 million increase in loans and a decrease of $1 million to the loan loss reserve, partially offset by $19 million in principal repayments. The entire commercial loan portfolio is U.S. based. As of March 31, 2012, the average total loan size was $1 million and the average loan participation size was less than $1 million. The number of loans in the portfolio increased from 3,272 at December 31, 2011 to 3,376 at March 31, 2012. Approximately 91% of the loans are full or partial recourse to borrowers.

Cash and cash equivalents as of March 31, 2012 were $5.410 billion, a decrease of $562 million or 9.4% from December 31, 2011. The decrease was primarily related to the investment of cash and cash equivalents associated with the QIL acquisition into fixed maturities.

Regarding fair value measurements, as of March 31, 2012, excluding separate accounts and other assets, the Company reflected $4.003 billion (6.1%) as level 1 (quoted prices in active markets) primarily consisting of U.S. Treasuries and common equity securities. The majority of the Company's invested assets are reported as level 2 (quoted prices from other observable inputs). As of March 31, 2012, the Company reported $59.776 billion (91.5%) as level 2, consisting primarily of various fixed maturity securities. Finally, the Company reported $1.545 billion (2.4%) as level 3 (unobservable inputs), primarily consisting of international and privately held securities for which a market price is not readily observable.

As of March 31, 2012, no single issuer, excluding U.S. Treasuries, agency securities and mortgage-backed securities, accounted for more than 1.5% of invested assets.

The following tables summarize the Company's available for sale portfolio by security type as of March 31, 2012 and December 31, 2011:

$ in Millions March 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	$2,810	$258	($1)	$3,067
Residential MBS [1]	8,600	534	(33)	9,101
Commercial MBS	2,084	78	(3)	2,159
Other MBS and ABS [2]	1,625	131	(2)	1,754
U.S. state and municipal	12,467	1,176	(18)	13,625
Corporate and other	25,632	1,731	(144)	27,219
Foreign government securities	5,481	170	(74)	5,577
Total fixed maturities	58,699	4,078	(275)	62,502
Common stock	1,618	338	(70)	1,886
Preferred stock	434	22	(61)	395
Total equity securities	2,052	360	(131)	2,281
Total securities available for sale	$60,751	$4,438	($406)	$64,783

1 Mortgage-backed securities ("MBS")
2 Asset-backed securities ("ABS")

$ in Millions December 31, 2011	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	$3,044	$312	($-)	$3,356
Residential MBS	9,018	525	(46)	9,497
Commercial MBS	2,086	74	(3)	2,157
Other MBS and ABS	1,645	132	(2)	1,775
U.S. state and municipal	12,530	1,159	(24)	13,665
Corporate and other	23,978	1,596	(319)	25,255
Foreign government securities	4,807	158	(94)	4,871
Total fixed maturities	57,108	3,956	(488)	60,576
Common stock	1,510	235	(137)	1,608
Preferred stock	432	17	(103)	346
Total equity securities	1,942	252	(240)	1,954
Total securities available for sale	$59,050	$4,208	($728)	$62,530

The following table summarizes the Company's mortgage and asset-backed fixed maturity portfolio by credit quality as of March 31, 2012:

$ in Millions	As of March 31, 2012							
Mortgage & Asset-Backed Fixed Maturities by Credit Quality[1]	**AAA**	**AA**	**A**	**BBB**	**BB**	**B or Lower**	**Total**	**% of Total**
SBA loans	$1,427	$-	$-	$-	$-	$-	$1,427	11.0%
GNMA residential mortgage	3,361	5	-	-	-	-	3,366	25.9
FNMA residential mortgage	2,807	-	-	-	-	-	2,807	21.6
FHLMC residential mortgage	2,384	-	-	-	-	-	2,384	18.3
Prime residential mortgage	27	34	21	14	5	224	325	2.5
Alt-A residential mortgage	-	2	28	8	8	125	171	1.3
Sub-prime residential mortgage	14	-	-	4	6	24	48	0.4
Commercial MBS	2,012	122	9	10	6	-	2,159	16.6
Non-mortgage ABS	187	22	25	70	7	16	327	2.4
Total	$12,219	$185	$83	$106	$32	$389	$13,014	100.0%
% of Total	93.9%	1.4%	0.6%	0.8%	0.3%	3.0%	100.0%	

[1]For purposes of this disclosure, credit quality is primarily based upon average credit ratings.

Approximately 77% of the Company's securitized portfolio is explicitly backed by the U.S. government (GNMA and SBA) or by government-sponsored entities (FHLMC and FNMA). Over 93% of the mortgage and asset-backed holdings are rated AAA. The commercial mortgage-backed securities portfolio is well diversified and of high quality with approximately 99% rated AA or above with 17% of the underlying collateral having been defeased with U.S. Treasuries.

The following table summarizes the Company's allocation of fixed maturities by credit quality as of March 31, 2012 and December 31, 2011:

$ in Millions	As of March 31, 2012		As of December 31, 2011	
Fixed Maturities by Credit Quality[1]	**Fair Value**	**% of Total**	**Fair Value**	**% of Total**
AAA	$21,418	34.3%	$21,732	36.0%
AA+, AA, AA-	10,249	16.4	10,445	17.2
A+, A, A-	12,495	20.0	11,646	19.2
BBB+, BBB, BBB-	11,707	18.7	10,289	17.0
BB+, BB, BB-	2,313	3.7	2,202	3.6
B+, B, B-	3,401	5.4	3,330	5.5
CCC or lower	919	1.5	932	1.5
Total fixed maturities	$62,502	100.0%	$60,576	100.0%

[1]For purposes of this disclosure, credit quality is primarily based upon average credit ratings.

The Company's allocation to investment grade securities as of March 31, 2012 remained consistent with December 31, 2011 at 89%. Overall, the average credit quality rating stands at A+ as of March 31, 2012. The Company's holdings of below investment grade securities primarily consist of an actively managed diversified portfolio of high yield securities and loans within the domestic insurance portfolios and investments in emerging market sovereign and corporate debt primarily in support of the Company's international insurance companies.

The following table summarizes the Company's allocation of fixed maturities by maturity date as of March 31, 2012 and December 31, 2011:

$ in Millions	As of March 31, 2012		As of December 31, 2011	
Fixed Maturities by Maturity Date	**Fair Value**	**% of Total**	**Fair Value**	**% of Total**
1 year or less	$2,953	4.7%	$2,847	4.7%
Over 1 year through 5 years	18,847	30.2	17,738	29.3
Over 5 years through 10 years	15,704	25.1	14,489	23.9
Over 10 years	11,984	19.2	12,073	19.9
MBS and ABS	13,014	20.8	13,429	22.2
Total fixed maturities	$62,502	100.0%	$60,576	100.0%

During 2012, after taking into consideration changes in investment opportunities and its view of the current and prospective business and economic environment, the Company made only minor adjustments to the average duration of its investment portfolio.

Net Investment Income

The following table summarizes the Company's net investment income for the three months ended March 31, 2012 and 2011:

$ in Millions	Three Months Ended March 31,	
Net Investment Income	**2012**	**2011**
Taxable interest income	$635	$598
Tax-exempt interest income	116	117
Dividends	11	11
LP and LLC income	121	210
Commercial mortgage loans	19	19
Other investment (loss) income	(4)	2
Gross investment income	898	957
Investment expenses	(36)	(42)
Net investment income	$862	$915

Net investment income for the three months ended March 31, 2012 was $862 million, a decrease of $53 million from the same period in 2011. The change in the period primarily reflects valuation changes in LP and LLC investments, partially offset by increases in taxable interest income due to a higher invested asset base as a result of the acquisition of QIL and continued reinvestment of cash flow from operations.

Net Realized Gains (Losses)

The following tables summarize the Company's net realized gains (losses) for the three months ended March 31, 2012 and 2011:

$ in Millions Net Realized Gains (Losses)	Sales & Dispositions	Impairments	Change in Derivatives Value	Total
Three Months Ended March 31, 2012:				
Fixed maturities	$53	($14)	$-	$39
Common and preferred stock	23	(11)	-	12
Other	(2)	-	-	(2)
Total	$74	($25)	$-	$49
Three Months Ended March 31, 2011:				
Fixed maturities	$43	($18)	$-	$25
Common and preferred stock	40	-	-	40
Other	11	-	-	11
Total	$94	($18)	$-	$76

$ in Millions	Three Months Ended March 31,	
Components of Net Realized Gains (Losses)	**2012**	**2011**
Fixed maturities:		
Gross realized gains	$65	$54
Gross realized losses	(26)	(29)
Equities:		
Gross realized gains	27	41
Gross realized losses	(15)	(1)
Other:		
Gross realized gains	1	19
Gross realized losses	(3)	(8)
Total net realized gains	$49	$76

Net realized gains for the three months ended March 31, 2012 were $49 million, a decrease of $27 million from the same period in 2011. The decrease was primarily related to higher other-than-temporary impairments and lower gains in 2012 on common equities as well as gains associated with fair value option elections recognized in 2011 that did not recur in 2012. The decrease was partially offset by gains recognized in connection with the sale of fixed maturity securities.

The following table summarizes the Company's unrealized losses and fair value by security type and by duration that individual securities have been in an unrealized loss position as of March 31, 2012 that are not deemed to be other-than-temporarily impaired:

$ in Millions	**Less Than 12 Months**		**12 Months or Longer**	
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. Government and agency securities	($1)	$145	$-	$-
Residential MBS	(3)	158	(30)	326
Commercial MBS	(2)	221	(1)	39
Other MBS and ABS	-	43	(2)	11
U.S. state and municipal	(4)	169	(14)	75
Corporate and other	(63)	2,440	(81)	783
Foreign government securities	(10)	634	(64)	567
Total fixed maturities	(83)	3,810	(192)	1,801
Common stock	(44)	417	(26)	147
Preferred stock	(1)	4	(60)	269
Total equities	(45)	421	(86)	416
Total	($128)	$4,231	($278)	$2,217

Unrealized losses decreased from $728 million as of December 31, 2011 to $406 million as of March 31, 2012 primarily due to improvement in the equity markets and the tightening of credit spreads. Unrealized losses less than 12 months decreased from $311 million at December 31, 2011 to $128 million as of March 31, 2012. Unrealized losses 12 months or longer decreased from $417 million as of December 31, 2011 to $278 million as of March 31, 2012. As of March 31, 2012, there were 779 securities that were in an unrealized loss position for 12 months or longer. The Company monitors the difference between the amortized cost and estimated fair value of debt securities to ascertain whether declines in value are temporary in nature. The Company currently does not have the intent to sell these securities and has determined it is not more likely than not that it would be required to sell these fixed income securities before they recover their fair value.

If the Company believes a decline in the value of a particular investment is temporary, the decline is recorded as an unrealized loss in policyholders' equity. If the decline is believed to be other-than-temporary, and the Company believes that it will not be able to collect all cash flows due on its fixed income securities, then the carrying value of the investment is written down to the expected cash flow amount and a realized loss is recorded as a credit impairment. A non-credit impairment loss is recognized in other comprehensive income, net of applicable taxes, as the difference between expected cash flows and fair value. For the three months ended March 31, 2012, the Company recorded $14 million of fixed maturity impairment losses. The Company has concluded that the remaining gross unrealized losses of fixed maturity securities as of March 31, 2012 are temporary.

For equity securities, if the decline is believed to be other-than-temporary, the carrying value of the investment is written down to fair value and a realized loss is recorded. The gross unrealized losses recorded on equity securities at March 31, 2012 resulted primarily from decreases in quoted fair 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. For the three months ended March 31, 2012, the Company recorded $11 million in impairment losses on equity securities. The Company has concluded that the gross unrealized losses of equity securities as of March 31, 2012 are temporary.

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 while keeping a certain amount in cash and short-term investments to meet unpredictable cash obligations. 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 March 31, 2012 (including cash and cash equivalents) totaled $75.874 billion.

Short-term debt and current maturities of long-term debt outstanding as of March 31, 2012 and December 31, 2011 were as follows:

$ in Millions	**As of March 31, 2012**	**As of December 31, 2011**
Commercial paper	$88	$-
Current maturities of long-term debt[1]	205	205
Total short-term debt and current maturities of long-term debt	$293	$205

[1] Reflects $204 million of debt originally issued by Safeco. On December 29, 2008, $187 million of the outstanding $204 million 7.25% notes due 2012 were exchanged for a like principal amount of newly issued LMGI notes.

Long-term debt outstanding as of March 31, 2012 and December 31, 2011 was as follows:

$ in Millions	As of March 31, 2012	As of December 31, 2011
8.00% Notes, due 2013	$260	$260
7.86% Medium term notes, due 2013	25	25
5.75% Notes, due 2014	500	500
7.30% Notes, due 2014	200	200
5.588% Mortgage loan due 2015	48	48
6.70% Notes, due 2016	249	249
7.00% Junior Subordinated notes, due 2067[1]	300	300
5.00% Notes, due 2021	600	600
8.50% Surplus notes, due 2025	140	140
7.875% Surplus notes, due 2026	227	227
7.625% Notes, due 2028	3	3
3.91% - 4.24% Federal Home Loan Bank Borrowings due 2032	277	-
7.00% Notes, due 2034	231	231
6.50% Notes, due 2035	471	471
7.50% Notes, due 2036	19	19
7.80% Junior Subordinated notes, due 2087[2]	700	700
10.75% Junior Subordinated notes, due 2088[3]	942	981
7.697% Surplus notes, due 2097	435	435
Subtotal	5,627	5,389
Unamortized discount	(47)	(48)
Total long-term	$5,580	$5,341

[1] The par value call date and final fixed rate interest payment date is March 15, 2017, subject to certain requirements.
[2] The par value call date and final fixed rate interest payment date is March 15, 2037, subject to certain requirements.
[3] The par value call date and final fixed rate interest payment date is June 15, 2038, subject to certain requirements.

As part of its overall capital strategy, the Company previously announced that it may issue, repurchase or exchange debt depending on market conditions. Debt repurchases may be done through open market or other appropriate transactions. The Company continues to evaluate market conditions and may periodically effect transactions in its debt, subject to applicable limitations.

Debt Transactions and In-force Credit Facilities

During the three month period ending March 31, 2012 and 2011, the Company repurchased $39 million and zero, respectively, of the 10.75% Junior Subordinated notes due 2088. Pre-tax losses of $15 million and zero, respectively, were recorded on these transactions and are included in loss on extinguishment of debt in the accompanying consolidated statements of income.

Liberty Mutual Insurance Company ("LMIC"), Peerless Insurance Company ("PIC") and Liberty Life Assurance Company of Boston ("LLAC") are members of the Federal Home Loan Bank of Boston. Liberty Mutual Fire Insurance Company ("LMFIC") became a member of the Federal Home Loan Bank of Chicago on January 11, 2012. Membership provides the Company with access to secured asset-based borrowings with loan maturities of up to 30 years. The combined estimated borrowing capacity of the four entities is $5.2 billion. On March 21, 2012, LMFIC borrowed $150 million at a rate of 3.91% with a maturity date of March 22, 2032. On March 23, 2012 and April 2, 2012, LMIC borrowed $127 million at a rate of 4.24% with a maturity date of March 23, 2032 and $23 million at a rate of 4.25% with a maturity date of April 2, 2032, respectively.

On October 24, 2011, LMAC and Ohio Casualty Corporation terminated their $200 million unsecured three-year revolving credit facility with a syndicate of lenders.

On October 17, 2011, LMGI entered into a five-year $750 million unsecured revolving credit facility which terminates on October 17, 2016. To date, no funds have been borrowed under the facility. In connection with the new facility, LMGI terminated its $400 million unsecured revolving credit facility.

The Company places commercial paper through a program issued by LMGI and guaranteed by LMIC. Effective October 17, 2011, the $400 million commercial paper program was increased to $750 million and is backed by the five-year $750 million unsecured revolving credit facility. As of March 31, 2012, there was $88 million of commercial paper outstanding.

On May 18, 2011, LMGI issued Senior Notes due 2021 (the "2021 Notes") with a face amount of $600 million. Interest is payable semi-annually at a fixed rate of 5.00%. The 2021 Notes mature on June 1, 2021.

On March 21, 2011, the Company announced a tender offer for its 7.50% Senior Notes due 2036 (the "2036 Notes"). On April 15, 2011, the Company paid approximately $449 million in connection with such tender offer, including approximately $5 million in accrued and unpaid interest, to holders of the 2036 notes tendered in such tender offer. Subsequent to the closing of the tender offer, the Company made an open market purchase of $5 million aggregate principal amount of the 2036 Notes. As a result of these transactions, the Company recorded a $40 million pre-tax loss in 2011. After completion of the tender offer and subsequent open market purchase, $19 million aggregate principal amount of the 2036 Notes remains outstanding.

As of March 31, 2012, the Company has a $1 billion three-year committed repurchase agreement maturing in 2013. As of March 31, 2012, no borrowings were outstanding under the agreement.

On March 26, 2010, LMIC entered into a $750 million three-year committed repurchase agreement. In connection with the new repurchase agreement, LMIC terminated its existing $750 million 364-day committed repurchase agreement. As of March 31, 2012, no borrowings were outstanding under the agreement.

On March 26, 2010, PIC entered into a $250 million three-year committed repurchase agreement. The repurchase agreement is guaranteed by LMIC. To date, no funds have been borrowed under the agreement.

On December 10, 2009, Berkeley/St. James Real Estate LLC, a wholly-owned affiliate of the Company, entered into a five-year $50 million mortgage loan secured by the Company's headquarters located at 175 Berkeley Street and 30 St. James Avenue, Boston, Massachusetts. The mortgage loan has limited recourse to Berkeley/St. James Real Estate LLC in certain instances and LMGI guarantees those limited recourse obligations.

Liberty Mutual Insurance Europe Limited's £10 million overdraft facility expired on March 31, 2012.

Interest Expense

Consolidated interest expense for the three months ended March 31, 2012 was $104 million, a decrease of $9 million from the same period in 2011. The decrease reflects the completion of the tender offer on the 2036 Notes, the repurchases of the 10.75% Junior Subordinated notes due 2088 and increased capitalized interest associated with the construction of the Company's new building, partially offset by the issuance of the 2021 Notes. The annual run-rate savings related to the debt tender, repurchases, 2021 Notes and FHLB borrowings is $22 million. As previously discussed, the Company continues to evaluate market conditions and may periodically effect transactions in its debt, subject to applicable limitations. Debt repurchases may be done through open market or other appropriate transactions.

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 March 31, 2012, the Company, through its downstream subsidiary LMGI, had $4.889 billion of debt outstanding, excluding discount. This amount includes a short-term loan of $137 million from LMIC with a maturity date of May 31, 2012.

The insurance subsidiaries' ability to pay dividends on preferred or common stock is restricted under applicable insurance laws and regulations and may be paid only from unassigned surplus. 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 policyholders, following such dividend, is reasonable in relation to its outstanding liabilities, is adequate to meet its financial needs, and does not exceed the insurer's unassigned surplus. 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, 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 LMFIC and Employers Insurance Company of Wausau ("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 its debt, as could a redomestication, merger or consolidation of LMIC, LMFIC or EICOW to a different domiciliary state.

The authorized control level risk-based capital (as of December 31, 2011) and 2012 available dividend capacity prior to needing regulatory approval for LMIC, LMFIC and EICOW were as follows:

$ in Millions	**RBC Ratio[1]**		**Dividend Capacity[2]**	**Dividends Paid[3]**
RBC Ratios and Dividend Capacity	**2011**	**2010**	**2012**	**2012**
LMIC	469%	503%	$1,359	$16
LMFIC	458%	551%	-	$4
EICOW	623%	671%	$49	-

[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.
[3] Dividends paid represent amounts paid during the three months ended March 31, 2012. Available dividend capacity as of March 31, 2012 is calculated as 2012 dividend capacity less dividends paid for the preceding 12 months. Dividends paid April 1, 2011 through March 31, 2012 for LMIC, LMFIC and EICOW were $65 million, $65 million and $50 million, respectively.

LMGI also has access to the following sources of funding:

- A management services agreement with LMIC pursuant to which LMGI is entitled to collect certain costs plus a management fee for services rendered by LMGI employees.
- Investment management agreements with affiliated entities pursuant to which an LMGI subsidiary registered investment advisor is entitled to recover annual expenses for investment management services performed by its employees.
- Liberty Corporate Services LLC ("LCS"), which through its subsidiaries collects fees and other revenues, primarily for claims administration and agency services rendered for affiliated and non-affiliated entities. For the three months ended March 31, 2012, LCS recorded $101 million in pre-tax income.

- Approximately $80 million of annual dividends related to non-redeemable perpetual preferred stock issuances by LMIC and LMFIC.

Statutory Surplus

Statutory surplus as regards policyholders for the combined operations of LMIC and its U.S affiliates, including international branches, was $16.525 billion and $15.701 billion at March 31, 2012 and December 31, 2011, respectively. The increase in surplus primarily reflects net income of $329 million (the sum of earnings from the Company's 58 domestic insurance companies and dividends from subsidiaries), unaffiliated unrealized gains of $327 million, and affiliated unrealized gains of $224 million, partially offset by other changes in surplus of ($56) million, primarily related to an increase in non-admitted assets.

CRITICAL ACCOUNTING POLICIES

Critical Accounting Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The Company's principal estimates include (1) unpaid claims and claim adjustment expense reserves, including asbestos and environmental liability reserves and loss sensitive premium attributable to prior years; (2) reinsurance recoverables and associated uncollectible allowance; (3) fair value determination and other-than-temporary impairments of the investment portfolio; (4) deferred acquisition costs; (5) valuation of goodwill and intangible assets; and (6) deferred income tax valuation allowance.

While the amounts included in the consolidated financial statements reflect management's best estimates and assumptions, these amounts ultimately could vary.

Certain reclassifications have been made to the 2011 amounts to conform with the 2012 presentation.

Adoption of New Accounting Standards

Effective January 1, 2012, the Company adopted the Financial Accounting Standards Board ("FASB") Accounting Standards Update 2010-26, *Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts* ("ASU 2010-26"). This guidance, as codified in FASB Accounting Standards Codification ("ASC") 944, *Financial Services - Insurance,* specifies that acquisition costs should include only those costs that are directly related to the acquisition or renewal of insurance contracts. All other acquisition related costs, including market research, training, administration, unsuccessful acquisition or renewal efforts, and product development, should be charged to expense as incurred. Either prospective or retrospective application is permitted. The Company elected to apply the guidance retrospectively, and the cumulative effect of the change in the method of accounting resulted in a decrease in the opening balance of total equity as of January 1, 2012 of $265 million, net of tax.

As of March 31, 2011, the accounting change resulted in increases (decreases) in deferred income taxes, deferred acquisition costs, unpaid claims and claim adjustment expenses and future policy benefits, other liabilities, unassigned equity, and accumulated other comprehensive income of $134 million, $(365) million, $34 million, $(4) million, $(267) million, and $6 million, respectively. For the period ended March 31, 2011, the accounting change resulted in (decreases) increases in benefits, claims and claim adjustment expenses, insurance operating costs and expenses, amortization of deferred policy acquisition costs, income tax expense, unrealized gains on securities, and foreign currency translation and other adjustments of $(1) million, $166 million, $(168) million, $1 million, $2 million, and $(2) million, respectively.

Effective January 1, 2012, the Company adopted ASU 2011-05, *Comprehensive Income* ("ASU 2011-05"). This guidance requires companies to present the total of comprehensive income, components of net income, and components of other comprehensive income ("OCI") in one continuous statement or in two separate but consecutive statements. The Company has elected to present this financial information in two separate, consecutive statements.

None of the accounting standards issued for the first quarter of 2012 will have a material impact on the Company.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were $50.469 billion and $50.228 billion as of March 31, 2012 and December 31, 2011, 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 litigation, medical costs, the costs of repair materials, and labor rates can all affect ultimate claim costs. In addition, time can be a critical part of reserving determinations since the longer the span between the incidence of a loss and the payment or settlement of the claim, the more variable the ultimate settlement can be. 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 reserves for unpaid claims and claim adjustment expenses, net of reinsurance decreased $49 million from $1.332 billion as of December 31, 2011 to $1.283 billion as of March 31, 2012.

In the third quarter of 2011, the Company completed ground-up asbestos and environmental reserve studies. The studies were completed by a multi-disciplined team of internal claims, legal, reinsurance and actuarial personnel, and they included all major segments of the Company’s direct, assumed, and ceded asbestos and environmental claims. As part of the internal reviews, potential exposures of certain policyholders were individually evaluated using the Company's proprietary stochastic model, which is consistent with published actuarial papers on asbestos reserving. Among the factors reviewed in depth by the team of specialists were the type of business, level of exposure, coverage limits, geographic distribution of products, types of injury, state jurisdictions, legal defenses, and reinsurance potential. The remaining policyholders (those with less potential exposure) were evaluated using aggregate methods that utilized information and experience specific to these insureds. The studies resulted in an increase to reserves of $338 million.

All asbestos and environmental 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. In addition, the Company acquired PruPac in 2003 and any increase in asbestos and environmental reserves is reinsured by Vantage Casualty Insurance Company and guaranteed by Prudential Financial, Inc.

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 $13.224 billion and $13.272 billion at March 31, 2012 and December 31, 2011, respectively, net of allowance for doubtful accounts of $294 million and $326 million, respectively. Included in these balances are $869 million and $941 million of paid recoverables and $12.649 billion and $12.657 billion of unpaid recoverables, respectively.

The Company's reinsurance recoverables from Nationwide Indemnity Company have been fully guaranteed by its parent, Nationwide Mutual Insurance Company, which has a financial strength rating of A+ from Standard & Poor's and A+ from A.M. Best. The reinsurance recoverables from state mandated involuntary pools and associations primarily 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. Reinsurer credit risk with respect to any such involuntary pool or association is a function of the creditworthiness of all the pool participants.

As part of its reinsurance security oversight, the Company has established a Reinsurance Credit Committee 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 committee is directly responsible for establishing the rating, collateral, and diversification requirements governing the Company's purchase and use of reinsurance.

Approximately 95% and 93% of the Company's reinsurance recoverable balance, net of collateral held and including voluntary and involuntary pools and associations, was from reinsurers rated A- or better from A.M. Best and Standard & Poor's, respectively, at March 31, 2012. Collateral held against outstanding gross reinsurance recoverable balances was $4.792 billion and $4.699 billion at March 31, 2012 and December 31, 2011, respectively.

The remaining 5% and 7% of the Company's net reinsurance recoverable balance is well diversified. No single reinsurer rated B++ or below by A.M. Best or below A- by Standard & Poor's accounts for more than 2% of GAAP equity. In addition, the average net reinsurance recoverable balance from individual reinsurers rated below A- or not rated by A.M. Best and Standard & Poor's was approximately $1 million as of March 31, 2012.

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 charges to the consolidated statement of operations.

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 7.8% annually. These contracts resulted in deferred gains (including experience related profit accruals of $113 million) that are amortized into income using the effective interest method over the estimated settlement periods. As of March 31, 2012, and December 31, 2011,

deferred gains related to these reinsurance arrangements were $308 million and $315 million, respectively, and are included in other liabilities within the consolidated balance sheets. Interest credited to the funds held balances for the three months ended March 31, 2012 and 2011 was $20 million and $30 million, respectively. Deferred gain amortization was $10 million and $99 million for the three months ended March 31, 2012 and 2011, respectively. Reinsurance recoverables related to these transactions, including experience related profit accruals, were $1.211 billion and $1.217 billion as of March 31, 2012, and December 31, 2011, respectively. Effective March 31, 2011, the Company commuted two workers compensation excess of loss retroactive reinsurance agreements. The commutations, which represent the complete and final settlement and discharge of all present and future obligations between the parties arising out of the agreements, resulted in a gain to the Company of $54 million, net of tax.

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 material contract change at the January 1, 2002 renewal, any premium and loss activity subsequent to December 31, 2001 is accounted for as retroactive reinsurance for coverage provided from the fourth quarter 2000 through the fourth quarter 2001 covered accident year periods. The retroactive portion of the aggregate stop loss program is included in the amounts disclosed in the preceding paragraph.

In 2009, the Company entered into a multi-year property catastrophe agreement with Mystic Re II Ltd. ("Mystic II"), a Cayman Islands domiciled reinsurer, to provide $225 million of reinsurance coverage for the Company and its affiliates in the event of a U.S. hurricane or earthquake event. The reinsurance agreement is collateralized. Such collateral is provided by Mystic II using proceeds from the issuance of certain catastrophe bonds. The reinsurance agreement provides coverage for hurricane or earthquake-related losses based on industry insured losses as reported by Property Claim Services along with company specific losses on the event. The 2009 reinsurance agreement terminated on March 13, 2012. Since no recoveries were recorded under this program, the associated collateral was released.

On March 6, 2012, the Company entered into two multi-year property catastrophe reinsurance agreements with Mystic Re III Ltd. ("Mystic III"), a Cayman Islands domiciled reinsurer, to provide $275 million of reinsurance coverage for the Company and its affiliates for a U.S. hurricane or earthquake event. The reinsurance agreements are collateralized. Such collateral is provided by Mystic III using proceeds from the issuance of certain catastrophe bonds. The reinsurance agreements provide coverage based on actual reported losses by the Company and its affiliates. The Company has not recorded any recoveries under this program. Mystic III does not have any other reinsurance in force.

Impairment Losses on Investments

If the Company believes a decline in the value of a particular investment is temporary, the decline is recorded as an unrealized loss in policyholders' equity. If the decline is believed to be "other-than-temporary," and the Company believes that it will not be able to collect all cash flows due on its fixed income securities, then the carrying value of the investment is written down to the expected cash flow amount and a realized loss is recorded as a credit impairment. A non-credit impairment loss is recognized in other comprehensive income, net of applicable taxes as the difference between expected cash flow and fair value.

The Company reviews fixed income, public equity securities and private equity and private equity co-investment securities for impairment on a quarterly basis. Securities are reviewed for both quantitative and qualitative considerations including, but not limited to: (a) the extent of the decline in fair value below book value, (b) the duration of the decline, (c) significant adverse changes in the financial condition or near term prospects of the investment or issuer, (d) significant change in the business climate or credit ratings of the issuer, (e) general market conditions and volatility, (f) industry factors, and (g) the past impairment of the security holding or the issuer. For fixed maturity securities that the Company does not intend to sell or

for which it is more likely than not that the Company would not be required to sell before an anticipated recovery in value, the Company separates impairments into credit loss and non-credit loss components. The determination of the credit loss component of the impairment charge is based on the Company's best estimate of the present value of the cash flows expected to be collected from the debt security compared to its amortized cost and is reported as part of net realized gains. The non-credit component, the residual difference between the credit impairment component and the fair value, is recognized in other comprehensive income. The factors considered in making an evaluation for credit versus non-credit other-than-temporary impairment include the following: (a) failure of the issuer of the security to make scheduled interest or principal payments (including the payment structure of the debt security and the likelihood the issuer will be able to make payments that increase in the future), (b) performance indicators of the underlying assets in the security (including default and delinquency rates), (c) vintage, (d) geographic concentration, (e) industry analyst reports, sector credit ratings, and volatility of the security's fair value. In addition, the Company's accounting policy for other-than-temporary impairment recognition requires an other-than-temporary impairment charge be recorded when it is determined the security will be sold or it is more likely than not that the Company will be required to sell the security before recovery of the security's amortized cost basis (all debt securities and certain preferred equity securities) or the Company does not have the intent and ability to hold certain equity securities for a period of time that is sufficient to allow for any anticipated recovery in fair value.

Subsequent to March 31, 2012, the Company has not recognized any additional material other-than-temporary impairments.

Variable Interest Entities

The Company invests in energy, private equity and real estate limited partnerships and other entities subject to variable interest entity ("VIE") analysis under the VIE subsections of ASC 810, *Consolidation*. The Company analyzes each investment to determine whether it is a VIE, and if so, whether the Company is the primary beneficiary or a significant interest holder based on a qualitative and quantitative assessment. The Company evaluates the design of the entity, the risks to which the entity was designed to expose the variable interest holder and the extent of the Company's control of and variable interest in the VIE. As of March 31, 2012, the Company has determined that it is the primary beneficiary of one VIE in the energy investment sector, and as such, this VIE has been consolidated in the Company's financial statements. The carrying value of assets and liabilities, and the Company's maximum exposure to loss of the consolidated VIE is immaterial to the Company.

The Company has variable interests in VIEs for which it is not the primary beneficiary and accounts for these VIEs under the equity method in accordance with ASC 323, *Investments-Equity Method and Joint Ventures*. The VIEs are principally private equity limited partnerships in which the Company has invested as a passive limited partner. The partnerships were deemed to be VIEs because the equity holders as a group lack the power to direct the activities that most significantly impact the respective entity's economic performance. The VIEs generate variability primarily from investment portfolio performance and that variability is passed to equity holders. For these VIEs, the Company absorbs a portion, but not majority, of this variability. The carrying value of assets was $288 million and $250 million as of March 31, 2012 and December 31, 2011, respectively and the Company's maximum exposure to loss was $450 million and $309 million as of March 31, 2012 and December 31, 2011, respectively for unconsolidated VIEs in which the Company has a significant variable interest. The assets are included in Other Investments on the consolidated balance sheets. Maximum exposure to loss includes the carrying value and unfunded commitment of the VIE. There is no recourse provision to the general credit of the Company for any VIE beyond the full amount of the Company's loss exposure.

Derivatives

The Company may enter into a derivative transaction through domestic insurance subsidiaries or non-insurance subsidiaries. Each domestic insurance subsidiary that has entered into derivative transactions has a Derivative Use Policy, which has been approved by its board of directors, and its derivative transactions are only entered into pursuant to such policy. Derivative transactions entered into by a non-insurance subsidiary are only entered into after approval by its board of directors.

Deferred Acquisition Costs

Total deferred acquisition costs were $2.479 billion and $2.808 billion as of March 31, 2012 and December 31, 2011, respectively. Deferred acquisition costs are costs that are directly related to the acquisition or renewal of insurance contracts. All other acquisition related costs, including market research, training, administration, unsuccessful acquisition or renewal efforts, and product development, should be charged to expense as incurred. 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 and underwriting expenses.

Goodwill

Goodwill assets were $4.817 billion and $4.766 billion as of March 31, 2012 and December 31, 2011, respectively. Goodwill is tested for impairment at least annually using either a qualitative or a quantitative process. Election of the approach can be made at the reporting unit level. The reporting unit has the option to skip the qualitative test and move directly to completion of the quantitative process. The Company's SBUs are deemed reporting units. The Company utilizes the qualitative and quantitative approaches across its business units.

The qualitative approach can be used to evaluate if there are any indicators of impairment. Through this process, the reporting unit must determine if there is indication that it is more likely than not that the fair value of the reporting unit is less than its carrying amount, including goodwill. If it is determined that there is an indication of potential impairment, the reporting unit must complete the quantitative process. The quantitative approach is a two-step process. The first step is performed to identify potential impairment and, if necessary, the second step is performed for the purpose of measuring the amount of impairment, if any. Impairment is recognized only if the carrying amount is not recoverable from the discounted cash flows using a "market" rate and is measured as the difference between the carrying amount and the implied fair value. Other changes in the carrying amount of goodwill are primarily caused by foreign currency translation adjustments and acquisitions.

Income Taxes

The net deferred income tax asset was $656 million and $815 million, net of a valuation allowance of $143 million and $136 million as of March 31, 2012 and December 31, 2011, respectively. The net decrease in the Company's net deferred income tax asset for the three months ended March 31, 2012 is primarily due to the change in net unrealized capital gains and losses on certain investments. The increase in the valuation allowance is primarily due to net operating losses generated in certain foreign subsidiaries where there is uncertainty in the timing and amount of the realization of those losses, and currency translation adjustments. Management believes it is more likely than not that the Company's net deferred income tax asset will be realized based on the Company's ability and likelihood of generating future taxable income.

The income tax provision is calculated under the liability method of accounting. Deferred income tax assets are recorded based upon 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 net

unrealized capital gains and losses on certain investments, insurance loss reserves, unearned premiums, deferred policy acquisition costs, employee benefits, net operating losses and intangible assets.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (amounts in millions):

Balance at December 31, 2011	$332
Additions for tax positions of prior years	19
Settlements	(9)
Balance at March 31, 2012	$342

Included in the tabular roll forward of unrecognized tax benefits is interest and penalties in the amount of $88 million and $78 million as of March 31, 2012 and December 31, 2011, respectively.

Included in the balance at March 31, 2012, is $164 million related to tax positions that would impact the effective tax rate.

The Company recognizes interest and penalties related to unrecognized tax benefits in Federal, state, and foreign income tax expense. During the three months ended March 31, 2012 and 2011, the Company recognized approximately $10 million and $4 million in interest and penalties, respectively. The Company had approximately $92 million and $82 million of interest and penalties accrued at March 31, 2012 and December 31, 2011, respectively.

The Company does not expect any material changes to the unrecognized tax benefits within 12 months of the reporting date.

The IRS has completed its review of the Company's federal income tax returns through the 1998 tax year and is currently reviewing income tax returns for the 1999 through 2009 tax years. Any adjustments that may result from the IRS examinations of these income tax returns are not expected to have a material impact on the financial position, liquidity, or results of operations of the Company.

About the Company

Boston-based LMHC, the parent corporation of the Liberty Mutual Insurance group of entities, is a diversified global insurer and third largest property and casualty insurer in the U.S. based on 2011 direct written premium. The Company also ranks 82nd on the Fortune 100 list of largest corporations in the United States based on 2010 revenue. As of December 31, 2011, LMHC had $117.131 billion in consolidated assets, $99.267 billion in consolidated liabilities, and $34.671 billion in annual consolidated revenue.

LMHC, 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 LMHC.

Functionally, the Company conducts substantially all of its business through four strategic business units: LMAC, International, Personal Markets and Commercial Markets. 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.

LMHC employs more than 45,000 people in more than 900 offices throughout the world. For a full description of the Company's business operations, products and distribution channels, please visit Liberty Mutual's Investor Relations web site at www.libertymutual.com/investors.