Liberty Mutual Holding Company Inc.

First Quarter 2017

Consolidated Financial Statements

Liberty Mutual Holding Company Inc.

Consolidated Statements of Income

(dollars in millions)

(Unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
Revenues		
Premiums earned	$ 8,895	$ 8,464
Net investment income	766	687
Fee and other revenues	267	250
Net realized gains (losses)	169	(39)
Total revenues	10,097	9,362
Claims, Benefits and Expenses		
Benefits, claims and claim adjustment expenses	6,544	5,731
Operating costs and expenses	1,640	1,587
Amortization of deferred policy acquisition costs	1,238	1,270
Interest expense	108	109
Interest credited to policyholders	68	67
Total claims, benefits and expenses	9,598	8,764
Loss on extinguishment of debt	(1)	(8)
Ironshore acquisition costs	(10)	-
Income before income tax expense and non-controlling interest	488	590
Income tax expense	137	187
Consolidated net income	351	403
Less: Net income attributable to non-controlling interest	-	10
Net income attributable to Liberty Mutual Holding Company Inc.	$ 351	$ 393

Net Realized Gains (Losses)

	2017	2016
Other-than-temporary impairment losses:		
Total other-than-temporary impairment losses	$ (45)	$ (17)
Change in portion of loss recognized in other comprehensive income	-	-
Other-than-temporary impairment losses	(45)	(17)
Other net realized gains (losses)	214	(22)
Net realized gains (losses)	$ 169	$ (39)

See accompanying notes to the unaudited consolidated financial statements.

Liberty Mutual Holding Company Inc.

Consolidated Statements of Comprehensive Income

(dollars in millions)

(Unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
Consolidated net income	$ 351	$ 403
Other comprehensive income, net of taxes:		
Unrealized gains on securities	237	695
Reclassification adjustment for (gains) and losses included in consolidated net income	(57)	10
Foreign currency translation and other adjustments	96	203
Other comprehensive income, net of taxes	276	908
Comprehensive income	$ 627	$ 1,311

See accompanying notes to the unaudited consolidated financial statements.

Liberty Mutual Holding Company Inc.

Consolidated Balance Sheets

(dollars in millions)

(Unaudited)

	March 31, 2017	December 31, 2016
Assets:		
Investments		
Fixed maturities, available for sale, at fair value (amortized cost of $63,194 and $63,169)	$ 64,904	$ 64,700
Equity securities, available for sale, at fair value (cost of $2,201 and $2,164)	2,705	2,576
Short-term investments	635	1,147
Commercial mortgage loans	2,665	2,582
Other investments	6,355	6,025
Total investments	77,264	77,030
Cash and cash equivalents	6,256	4,608
Premium and other receivables	10,936	10,649
Reinsurance recoverables	13,913	13,820
Deferred income taxes	213	402
Deferred acquisition costs	3,437	3,348
Goodwill	4,860	4,850
Prepaid reinsurance premiums	1,077	1,082
Other assets	10,611	9,803
Total assets	$ 128,567	$ 125,592
Liabilities:		
Unpaid claims and claim adjustment expenses and future policy benefits:		
Property and casualty	$ 50,277	$ 49,721
Life	10,042	9,833
Other policyholder funds and benefits payable	7,086	6,768
Unearned premiums	18,182	17,823
Funds held under reinsurance treaties	228	202
Long-term debt	8,146	7,603
Other liabilities	13,592	13,255
Total liabilities	107,553	105,205
Equity:		
Unassigned equity	22,021	21,670
Accumulated other comprehensive loss	(1,030)	(1,304)
Total policyholders' equity	20,991	20,366
Non-controlling interest	23	21
Total equity	21,014	20,387
Total liabilities and equity	$ 128,567	$ 125,592

See accompanying notes to the unaudited consolidated financial statements.

Liberty Mutual Holding Company Inc.

Consolidated Statements of Changes in Total Equity

(dollars in millions)

(Unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
Balance at beginning of the year	$ 20,387	$ 19,241
Comprehensive income:		
Consolidated net income	351	403
Other comprehensive income, net of taxes	276	908
Total comprehensive income	627	1,311
Distributions to non-controlling interest	-	(53)
Balance at end of the period	$ 21,014	$ 20,499

See accompanying notes to the unaudited consolidated financial statements.

Liberty Mutual Holding Company Inc.

Consolidated Statements of Cash Flows

(dollars in millions)

(unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
Cash flows from operating activities:		
Consolidated net income	$ 351	$ 403
Adjustments to reconcile consolidated net income to net cash provided by operating activities:		
Depreciation and amortization	175	205
Realized (gains) losses	(169)	39
Undistributed private equity investment gains	(153)	(60)
Premium, other receivables, and reinsurance recoverables	(707)	(377)
Deferred acquisition costs	(85)	(104)
Liabilities for insurance reserves	1,165	503
Taxes payable, net of deferred	101	162
Pension plan contributions	(401)	(101)
Other, net	(343)	(371)
Total adjustments	(417)	(104)
Net cash (used in) provided by operating activities	(66)	299
Cash flows from investing activities:		
Purchases of investments	(5,863)	(3,861)
Sales and maturities of investments	6,315	3,663
Property and equipment purchased, net	180	(156)
Cash paid for disposals and acquisitions, net of cash on hand	-	(130)
Other investing activities	141	292
Net cash provided by (used in) investing activities	773	(192)
Cash flows from financing activities:		
Net activity in policyholder accounts	261	124
Debt financing, net	534	(16)
Net security lending activity and other financing activities	130	(30)
Net cash provided by financing activities	925	78
Effect of exchange rate changes on cash	16	12
Net increase in cash and cash equivalents	1,648	197
Cash and cash equivalents, beginning of year	4,608	4,227
Cash and cash equivalents, end of period	$ 6,256	$ 4,424

See accompanying notes to the unaudited consolidated financial statements.

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying consolidated financial statements include the accounts of Liberty Mutual Holding Company Inc., entities over which the Company exercises control including majority and wholly owned subsidiaries, and variable interest entities ("VIE") when the Company is deemed the primary beneficiary (collectively "LMHC" or the "Company"). The minority ownership of consolidated affiliates is represented in equity as non-controlling interest. All material intercompany transactions and balances have been eliminated.

The accompanying consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP"). 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 and direct working interests in oil and gas properties, (4) recoverability of deferred acquisition costs, (5) valuation of goodwill and intangible assets, (6) deferred income tax valuation allowance, and (7) pension and postretirement benefit obligations. While the amounts included in the consolidated financial statements reflect management's best estimates and assumptions, these amounts ultimately could vary.

Adoption of Accounting Standards

The Company has not adopted any accounting standards through the first quarter of 2017.

Accounting Standards Not Yet Adopted

The Company will adopt the FASB issued ASU 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"). ASU 2014-09 was issued to clarify the principles for recognizing revenue, however, insurance contracts and financial instrument transactions are not within the scope of this guidance. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers,* which deferred the effective date of ASU 2014-09 by one year. Accordingly, ASU 2014-09 is effective for public business entities for annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. The Company is currently evaluating the impact the adoption of ASU 2014-09 is expected to have on the Company's financial statements. The standard is not expected to have a material impact on the Company.

The Company will adopt the FASB issued ASU 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* ("ASU 2016-01"). ASU 2016-01 requires equity investments (excluding those accounted for under the equity method or those that result in consolidation) to be measured at fair value, with changes in fair value recognized in net income. ASU 2016-01 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The Company is currently evaluating the impact of the adoption of ASU 2016-01. The adoption is expected to have a material impact on the Company's financial statements.

The Company will adopt the FASB issued ASU 2016-02, *Leases* ("ASU 2016-02"). The amendments will require a lessee to recognize a right-of-use asset and a lease liability on the balance sheet for leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The amendments of ASU 2016-02 are effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact the adoption of ASU 2016-02 is expected to have on the Company's financial statements.

The Company will adopt the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* ("ASU 2016-13"). ASU 2016-13 replaces the current incurred loss model with an expected credit loss model, which measures credit losses on financial instruments measured at amortized cost, and will require companies to recognize an allowance for expected credit losses. In addition, ASU 2016-13 also amends the credit loss measurement guidance for available-for-sale debt securities and beneficial interests in securitized financial assets. This amendment removes certain factors to consider when determining whether credit losses should be recognized and will require companies to recognize expected credit losses through an allowance. ASU 2016-13 is effective for public business entities for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently evaluating the impact of the adoption of ASU 2016-13. The impact on the Company's results of operations, financial position or liquidity at the date of adoption will be determined by the financial instruments held by the Company and the economic conditions at that time.

There are no other accounting standards not yet adopted by the Company that are expected to have a material impact.

(dollars in millions)

Securities Lending

The Company participates in a securities lending program to generate additional income, whereby certain domestic fixed maturity securities and equity securities are loaned for a short period of time from the Company's portfolio to qualifying third parties via a lending agent. Terms of the agreement are for borrowers of these securities to provide collateral of at least 102% of the market value of the loaned securities. Acceptable collateral may be in the form of cash or permitted securities as outlined in the securities lending agreement. The market value of the loaned securities is monitored and additional collateral is obtained if the market value of the collateral falls below 102% of the market value of the loaned securities. Under the terms of the securities lending program, the lending agent indemnifies the Company against borrower defaults. The loaned securities remain a recorded asset of the Company; however, the Company records a liability for the amount of cash collateral held, representing its obligation to return the collateral related to the loaned securities.

Net Investment Hedge Instruments

The Company has designated non-derivative foreign-currency denominated long-term debt and the related accrued interest as hedges of its net investment in certain foreign operations. Accordingly, the foreign currency translation of the debt instrument and accrued interest is recorded in accumulated other comprehensive income (loss), offsetting the foreign currency translation adjustment of the related net investment that is also recorded in accumulated other comprehensive income (loss). As of March 31, 2017, the Company had €1,250 million of outstanding long-term debt and approximately €19 million of accrued interest designated as non-derivative hedges of its net investment in certain foreign operations. The foreign currency translation of the debt instrument and accrued interest recorded in accumulated other comprehensive income (loss) was immaterial. (See Note 5 for further discussion.)

Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists principally of unrealized gains and losses on certain investments in debt and equity securities, foreign currency translation adjustments, and pension and postretirement liability adjustments.

The components of accumulated other comprehensive loss excluding non-controlling interest, net of related deferred acquisition costs and taxes, are as follows:

	March 31, 2017	December 31, 2016
Unrealized gains on securities	$1,142	$962
Foreign currency translation & other adjustments	(642)	(708)
Pension liability funded status	(1,530)	(1,558)
Accumulated other comprehensive loss	$(1,030)	$(1,304)

The following table presents the consolidated other comprehensive income reclassification adjustments for the three months ended March 31, 2017 and 2016, respectively.

Three months ended March 31, 2017	**Unrealized gains on securities**	**Change in pension and post retirement plans funded status**	**Foreign currency translation and other adjustments(1)**	**Total**
Unrealized change arising during the period	$368	$ -	$74	$442
Less: Reclassification adjustments included in consolidated net income	88	(42)	-	46
Total other comprehensive income before income tax expense	280	42	74	396
Less: Income tax expense	100	14	6	120
Total other comprehensive income, net of income tax expense	$180	$28	$68	$276

(1) Includes $2 of non-controlling interest.

(dollars in millions)

Three months ended March 31, 2016	Unrealized gains on securities	Change in pension and post retirement plans funded status	Foreign currency translation and other adjustments[(1)]	Total
Unrealized change arising during the period	$1,042	$ -	$186	$1,228
Less: Reclassification adjustments included in consolidated net income	(15)	(40)	-	(55)
Total other comprehensive income before income tax expense	1,057	40	186	1,283
Less: Income tax expense	352	14	9	375
Total other comprehensive income, net of income tax expense	$705	$26	$177	$908

(1) Includes $14 of non-controlling interest.

(2) ACQUISITIONS AND DISPOSITIONS

ACQUISITIONS

Ironshore Inc.
On December 5, 2016, the Company entered into an agreement to purchase Ironshore Inc. ("Ironshore") from Fosun International Ltd. Ironshore had approximately $2,200 of gross written premium in 2016. The transaction is subject to regulatory approval and expected to close in the first half of 2017. Transaction related costs primarily consist of non-recurring banking, legal, tax, and accounting expenses and are reflected on the consolidated statements of income separately.

Compañia de Seguros Generales Penta Security S.A.
On January 14, 2016, the Company completed the acquisition of Compañia de Seguros Generales Penta Security S.A., the fourth largest non-life insurer in Chile. Compañia de Seguros Generales Penta Security S.A. had approximately $160 of net written premium in 2015.

DISPOSITIONS

Liberty Ubezpieczenia
On September 30, 2016, the Company completed the sale of substantially all the assets and liabilities of its Polish operation resulting in an immaterial gain. Liberty Ubezpieczenia had approximately $90 of net written premium in 2015.

HELD FOR SALE

Liberty Insurance (China)
On August 16, 2016, the Company entered into an agreement to sell a 51% interest of its Chinese operations to Sanpower Group. The transaction is subject to regulatory approval. A gain is expected on the sale.

(dollars in millions)

(3) INVESTMENTS

The amortized cost, gross unrealized gains and losses and fair values of available for sale investments as of March 31, 2017 and December 31, 2016, are as follows:

March 31, 2017	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
U.S. government and agency securities	$3,027	$117	$(22)	$3,122
Residential MBS[1]	6,256	135	(46)	6,345
Commercial MBS	1,688	25	(6)	1,707
Other MBS and ABS[2]	2,752	39	(16)	2,775
U.S. state and municipal	13,542	485	(164)	13,863
Corporate and other	31,056	1,164	(173)	32,047
Foreign government securities	4,873	193	(21)	5,045
Total fixed maturities	63,194	2,158	(448)	64,904
Common stock	1,838	539	(25)	2,352
Preferred stock	363	14	(24)	353
Total equity securities	2,201	553	(49)	2,705
Total securities available for sale	$65,395	$2,711	$(497)	$67,609

December 31, 2016	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
U.S. government and agency securities	$3,141	$118	$(29)	$3,230
Residential MBS	6,554	147	(50)	6,651
Commercial MBS	1,659	25	(6)	1,678
Other MBS and ABS	2,966	37	(23)	2,980
U.S. state and municipal	14,014	462	(194)	14,282
Corporate and other	29,935	1,123	(233)	30,825
Foreign government securities	4,900	188	(34)	5,054
Total fixed maturities	63,169	2,100	(569)	64,700
Common stock	1,801	469	(31)	2,239
Preferred stock	363	15	(41)	337
Total equity securities	2,164	484	(72)	2,576
Total securities available for sale	$65,333	$2,584	$(641)	$67,276

[1] Mortgage-backed securities (“MBS”)
[2] Asset-backed securities (“ABS”)

Of the $2,352 and $2,239 of common stock as of March 31, 2017 and December 31, 2016, respectively, $575 and $538, respectively, related to securities associated with non-guaranteed unit linked products where the policyholder bears the investment risk.

As of March 31, 2017 and December 31, 2016, the fair values of fixed maturity securities and equity securities loaned were approximately $1,493 and $1,115, respectively. Cash and short-term investments received as collateral in connection with the loaned securities were approximately $1,320 and $898 as of March 31, 2017 and December 31, 2016, respectively. Investments other than cash and short-term investments received as collateral in connection with the loaned securities were approximately $218 and $250 as of March 31, 2017 and December 31, 2016, respectively.

(dollars in millions)

The fair value of fixed maturities as of March 31, 2017 and December 31, 2016, by contractual maturity are as follows:

	As of March 31, 2017	As of December 31, 2016
Due to mature:		
One year or less	$3,399	$3,323
Over one year through five years	18,349	17,696
Over five years through ten years	17,188	17,341
Over ten years	15,141	15,031
MBS and ABS of government and corporate agencies	10,827	11,309
Total fixed maturities	$64,904	$64,700

Expected maturities may differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Due to the potential for prepayment on MBS and ABS, they are not categorized by contractual maturity.

The following table summarizes the Company's gross realized gains and losses by asset type for the three months ended March 31, 2017 and 2016, respectively:

Components of Net Realized Gains (Losses)	2017	2016
Fixed maturities:		
Gross realized gains	$63	$33
Gross realized losses	(30)	(52)
Equities:		
Gross realized gains	66	109
Gross realized losses	(11)	(105)
Other:		
Gross realized gains	122	8
Gross realized losses	(41)	(32)
Total net realized gains (losses)	$169	$(39)

During the quarters ended March 31, 2017 and 2016, the Company recorded $(45) and $(17) of impairment losses, respectively. As of March 31, 2017 and December 31, 2016, other-than-temporary impairment losses recognized through accumulated other comprehensive income were $(30) and $(30), respectively.

During the quarters ended March 31, 2017 and 2016, proceeds from sales of fixed maturities available for sale were $2,914 and $829, respectively. The gross realized gains (losses) on sales of fixed maturities available for sale totaled $51 and $(15) in 2017 and $21 and $(44) in 2016. During the quarters ended March 31, 2017 and 2016, proceeds from sales of equities available for sale were $400 and $643, respectively. The gross realized gains (losses) on sales of equities available for sale totaled $61 and $(8) in 2017 and $88 and $(79) in 2016.

(dollars in millions)

The following tables summarize the gross unrealized losses and fair value of fixed income and equity securities by the length of time that individual securities have been in a continuous unrealized loss position as of March 31, 2017 and December 31, 2016, and that are not deemed to be other-than-temporarily impaired:

March 31, 2017	**Less Than 12 Months**		**12 Months or Longer**	
	Unrealized Losses	**Fair Value of Investments with Unrealized Losses**	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**
U.S. government and agency securities	$(22)	$1,693	$-	$5
Residential MBS	(45)	2,899	(1)	30
Commercial MBS	(6)	590	-	10
Other MBS and ABS	(11)	991	(5)	110
U.S. state and municipal	(158)	3,741	(6)	61
Corporate and other	(136)	6,708	(37)	635
Foreign government securities	(19)	1,178	(2)	104
Total fixed maturities	(397)	17,800	(51)	955
Common stock	(14)	227	(11)	85
Preferred stock	-	17	(24)	256
Total equities	(14)	244	(35)	341
Total	$(411)	$18,044	$(86)	$1,296

December 31, 2016	**Less Than 12 Months**		**12 Months or Longer**	
	Unrealized Losses	**Fair Value of Investments with Unrealized Losses**	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**
U.S. government and agency securities	$(28)	$1,774	$(1)	$6
Residential MBS	(49)	3,135	(1)	34
Commercial MBS	(6)	639	-	8
Other MBS and ABS	(18)	1,499	(5)	155
U.S. state and municipal	(188)	4,491	(6)	66
Corporate and other	(178)	7,878	(55)	840
Foreign government securities	(30)	1,425	(4)	263
Total fixed maturities	(497)	20,841	(72)	1,372
Common stock	(14)	187	(17)	164
Preferred stock	(1)	17	(40)	241
Total equities	(15)	204	(57)	405
Total	$(512)	$21,045	$(129)	$1,777

Unrealized losses decreased from $641 as of December 31, 2016 to $497 as of March 31, 2017. Unrealized losses less than 12 months decreased from $512 at December 31, 2016 to $411 as of March 31, 2017. Unrealized losses 12 months or longer decreased from $129 as of December 31, 2016 to $86 as of March 31, 2017. Of the $11 unrealized losses 12 months or longer on common stock, $3 relates to securities associated with non-guaranteed unit linked products where the policyholder bears the investment risk. As of March 31, 2017, there were 811 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 fixed maturity 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 maturity securities before they recover their fair value.

If the Company believes a decline in the value (including foreign exchange rates) of a particular fixed maturity security 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 maturity 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. The Company has concluded that the remaining gross unrealized losses of fixed maturity securities as of March 31, 2017 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 as of March 31, 2017 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. The Company has concluded that the gross unrealized losses of equity securities as of March 31, 2017 are temporary, and the Company has the intent and ability to hold these securities until recovery.

The Company reviews fixed maturity securities, equity securities and other investments for impairment on a quarterly basis. These investments 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, (g) the past impairment of the security holding or the issuer and (h) impact of foreign exchange rates on foreign currency denominated securities. 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 fixed maturity 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 fixed maturity 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 and (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 fixed maturity 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.

The Company is required to review its natural resource and other equity method investments when facts and circumstances indicate that carrying values may not be recoverable. In performing a quarterly review, the fair value of the Company's investment is estimated using indicators including, but not limited to, market comparables and analyses, commodity prices, and discounted cash flows and a realized loss is recognized for the excess, if any, of the investment's carrying value over its estimated fair value.

The Company is required to review its oil and gas properties when facts and circumstances indicate that net book values may not be recoverable. In performing a quarterly review, an undiscounted cash flow test is performed at the lowest level for which identifiable cash flows are independent of cash flows from other assets. If the sum of the undiscounted future net cash flows is less than the net book value of the property, an impairment loss is recognized for the excess, if any, of the property's net book value over its estimated fair value.

Variable Interest Entities

The Company invests in limited partnerships and other entities subject to 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, 2017 and December 31, 2016, the Company has determined that it is not the primary beneficiary of any of its VIEs except for the Company's investment in its India joint venture which is deemed immaterial.

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*. These 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. The net carrying value of non-consolidated VIEs in which the Company has a variable interest was $4,987 and $4,675 as of March 31, 2017 and December 31, 2016, respectively, and the Company's maximum exposure to loss was $7,669 and $7,477 as of March 31, 2017 and December 31, 2016, respectively. The assets are included in other investments on the accompanying consolidated balance sheets. Maximum exposure to loss includes the carrying value and unfunded commitment of the VIE. The increase in the maximum exposure to loss from December 31, 2016 to March 31, 2017 is primarily related to new investments made during the current period.

(4) REINSURANCE

In the ordinary course of business, the Company assumes reinsurance and also cedes reinsurance to other insurers to reduce overall risk, including exposure to large losses and catastrophic events. The Company is also a member of various involuntary pools and associations and serves as a servicing carrier for residual market organizations. The Company remains contingently liable in the event reinsurers are unable to meet their obligations for paid and unpaid reinsurance recoverables and unearned premiums ceded under reinsurance agreements.

The Company reported reinsurance recoverables of $13,913 and $13,820 as of March 31, 2017 and December 31, 2016, respectively, net of allowance for doubtful accounts of $234 and $235, respectively. Included in these balances are $557 and $564 of paid recoverables and $13,590 and $13,491 of unpaid recoverables, respectively.

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 accompanying consolidated statements of income.

On July 17, 2014, Liberty Mutual Insurance Company ("LMIC") entered into a reinsurance transaction with National Indemnity Company ("NICO"), a subsidiary of Berkshire Hathaway Inc., on a combined aggregate excess of loss agreement for substantially all of the Company's U.S. workers compensation, asbestos and environmental liabilities (the "NICO Reinsurance Transaction"), attaching at $12,522 of combined aggregate reserves, with an aggregate limit of $6,500 and sublimits of $3,100 for asbestos and environmental liabilities and $4,507 for certain workers compensation liabilities. At the closing of the NICO Reinsurance Transaction, but effective as of January 1, 2014, the Company ceded $3,320 of existing undiscounted liabilities under this retroactive reinsurance agreement. NICO will provide $3,180 of additional aggregate adverse development cover. The Company paid NICO total consideration of $3,046, and recorded a pre-tax loss of $128. With respect to the ceded asbestos and environmental business, NICO has been given authority to handle claims, subject to the Company's oversight and control. With respect to the ceded workers compensation business, the Company will continue to handle claims.

In general terms, the covered business includes post December 31, 2013 development on: (1) asbestos and environmental liabilities arising under policies of insurance and reinsurance with effective dates prior to January 1, 2005; and (2) workers compensation liabilities arising out of policies on the books of the Company's Commercial Insurance Strategic Business Unit as of December 31, 2013, as respects injuries or accidents occurring prior to January 1, 2014.

To the extent there is unfavorable development of losses covered by this reinsurance, additional reinsurance benefit is recognized in the consolidated statements of income until those benefits exceed the original loss on the transaction. Reinsurance benefits in excess of the original loss will be deferred and recognized over the claims paying period of the reinsured policies.

(dollars in millions)

As the aggregate of workers compensation and asbestos and environmental development has exceeded the original pre-tax loss of $128, deferred gains are now being recorded. Deferred gains are amortized into earnings over the period when underlying claims are settled. The Company reported deferred gain amortization of ($4) and $13 at March 31, 2017 and December 31, 2016, respectively. As of March 31, 2017 and December 31, 2016, deferred gains were $73 and $62, respectively, and are included in other liabilities within the accompanying consolidated balance sheets.

(5) DEBT OUTSTANDING

Debt outstanding as of March 31, 2017 and December 31, 2016 includes the following:

Long-term debt:

	2017	2016
Junior Subordinated Notes, due 2067[(1) (2)]	$300	$300
5.00% Notes, due 2021	600	600
4.95% Notes, due 2022	750	750
4.25% Notes, due 2023	1,000	1,000
1.75% €500 Notes, due 2024	535	-
8.50% Surplus Notes, due 2025	140	140
2.75% €750 Notes, due 2026	802	791
7.875% Surplus Notes, due 2026	227	227
7.625% Notes, due 2028	3	3
3.91% - 4.25% Federal Home Loan Bank Borrowings due 2032	300	300
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)]	66	68
6.50% Notes, due 2042	750	750
4.85% Notes, due 2044	1,050	1,050
7.697% Surplus Notes, due 2097	260	260
	8,204	7,660
Unamortized discount	(15)	(15)
Total long-term debt excluding unamortized debt issuance costs	8,189	7,645
Unamortized debt issuance costs	(43)	(42)
Total long-term debt	$8,146	$7,603

(1) 7.00% fixed rate became 6.324% starting March 15, 2017 through a swap. Bondholders will be paid 3-month LIBOR + 2.905%.
(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.

Debt Transactions and In-Force Credit Facilities

During the three months ended March 31, 2017, the Company repurchased $2 of the 10.75% Junior Subordinated notes due 2088 compared to repurchases of $16 in 2016. Pre-tax losses of $1 were recorded on these transactions for the three months ended March 31, 2017 compared to pre-tax losses of $8 in 2016 and are included in loss on extinguishment of debt in the accompanying consolidated statements of income.

On March 27, 2017, Liberty Mutual Finance Europe DAC issued €500 million par value of Senior Notes due 2024 (the "2024 Notes"). Interest is payable annually at a fixed rate of 1.75%. The 2024 Notes mature on March 27, 2024.

On May 5, 2016, LMIC extended the termination date of a $1,000 repurchase agreement from July 3, 2017 to July 3, 2018. At March 31, 2017, no funds were borrowed under the facility.

On May 4, 2016, Liberty Mutual Group Inc. ("LMGI") issued €750 million par value of Senior Notes due 2026 (the "2026 Notes"). Interest is payable annually at a fixed rate of 2.75%. The 2026 Notes mature on May 4, 2026.

On December 21, 2015, LMIC renewed a $1,000 repurchase agreement for a two-year period, which terminates December 21, 2017. At March 31, 2017, no funds were borrowed under the facility.

The Company places commercial paper through a program issued by LMGI and guaranteed by LMIC. On April 8, 2015, LMGI increased its commercial paper program from $750 to $1,000. As of March 31, 2017, there was no commercial paper outstanding.

On March 5, 2015, LMGI amended and restated its unsecured revolving credit facility from $750 to $1,000 with an expiration date of March 5, 2020. This facility backs the Company's commercial paper program. To date, no funds have been borrowed under the facility. LMIC, Peerless Insurance Company ("PIC"), Liberty Life Assurance Company of Boston ("LLAC"), Liberty Mutual Fire Insurance Company ("LMFIC"), and Employers Insurance Company of Wausau ("EICOW") are members of the Federal Home Loan Bank. On March 21, 2012, LMFIC borrowed $150 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 at a rate of 4.24% with a maturity date of March 23, 2032 and $23 at a rate of 4.25% with a maturity date of April 2, 2032, respectively. As of March 31, 2017, all of the outstanding Federal Home Loan Bank borrowings are fully collateralized.

On January 20, 2012, LMGI entered into two interest rate swap transactions having a notional amount of $300 with respect to LMGI's $300 7.00% Junior Subordinated Notes due 2067. Pursuant to the terms of the swap agreements, commencing on March 15, 2017 and effective through March 15, 2037, LMGI has agreed with the counterparties to pay a fixed rate of interest on the notional amount and the counterparties have agreed to pay a floating rate of interest on the notional amount.

Payments of interest and principal of the surplus notes are expressly subordinate to all policyholder claims and other obligations of LMIC. Accordingly, interest and principal payments are contingent upon prior approval of the Commissioner of Insurance of the Commonwealth of Massachusetts.

(6) UNPAID CLAIMS AND CLAIM ADJUSTMENT EXPENSES

The Company establishes reserves for payment of claims and claim adjustment expenses that arise from the policies issued. As required by applicable accounting rules, no reserves are established until a loss, including a loss from a catastrophe, occurs. The Company's reserves are segmented into three major categories: reserves for reported claims (estimates made by claims adjusters); incurred but not reported claims reserves ("IBNR") representing reserves for unreported claims and supplemental reserves for reported claims; and reserves for the costs to settle claims. The Company establishes its reserves net of salvage and subrogation by line of business or coverage and year in which losses occur.

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 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.

In order to establish a reserve for IBNR claims, the actuarial teams within each of the SBUs use their experience and knowledge of the lines of business to estimate the potential future development of the incurred claims. The Company uses a number of actuarial methods and assumptions to develop an estimate of ultimate claim liabilities. Generally, these are a combination of exposure and experience based actuarial methods and review of other pertinent and available information from claims, underwriting, product and finance. Exposure based actuarial methods consider historical loss ratios and adjust for rate changes, premium and loss trends, industry trends and other information. These methods are typically used when developing an actuarial central estimate for more recent policy periods when claims data is insufficient to produce a reliable indication. As claims data becomes more reliable for a given policy period, more consideration is given to experience methods which review and monitor actual paid and reported development.

A comprehensive actuarial reserve review is performed for each product line at least once a year. The process and methods used for each product line vary depending on the circumstances and include input from claims, underwriting, product and finance. Each quarter the actuarial central estimate for each product line is reviewed and updated based upon development and presented to the reserving committee to conclude on the Company's best estimate of ultimate claim liabilities.

(dollars in millions)

Activity in property and casualty unpaid claims and claim adjustment expenses of the Company are summarized as follows:

	2017	2016
Balance as of January 1	$49,721	$49,323
Less: unpaid reinsurance recoverables[1]	10,016	9,891
Net balance as of January 1	39,705	39,432
Balance attributable to acquisitions and dispositions[2]	-	55
Incurred attributable to:		
Current year	5,965	5,306
Prior years[3]	-	(53)
Discount accretion attributable to prior years	15	15
Total incurred	5,980	5,268
Paid attributable to:		
Current year	2,125	1,974
Prior years	3,454	3,178
Total paid	5,579	5,152
Amortization of deferred retroactive reinsurance gain	4	-
Net adjustment due to foreign exchange	69	91
Add: unpaid reinsurance recoverables[1]	10,098	9,999
Balance as of March 31	$50,277	$49,693

[1] In addition to the unpaid reinsurance recoverable balances noted above, and as a result of retroactive reinsurance agreements, the Company has recorded retroactive reinsurance recoverable balances of $3,152 and $3,006 as of March 31, 2017 and 2016, respectively.
[2] The balance attributable to acquisitions and dispositions primarily represents the disposition of Liberty Ubezpieczenia during the year ended 2016. (See Note 2 for further discussion.)
[3] Does not include increases (decreases) in allowance related to reinsurance recoverables due to prior year development of $2 and ($2) as of March 31, 2017 and 2016, respectively.

The change in incurred attributable to prior years, excluding asbestos and environmental and amortization of deferred retroactive gain, is primarily attributable to favorable development in the reinsurance line of business in 2016 that did not recur.

Asbestos and Environmental Reserves
The Company's asbestos and environmental reserves for unpaid claims and claim adjustment expenses, net of reinsurance before the NICO Reinsurance Transaction and including uncollectible reinsurance, were $909 and $936 as of March 31, 2017 and December 31, 2016, respectively.

(7) INCOME TAXES

The income tax provision is calculated under the liability method of accounting. The Company recognizes deferred income tax assets and liabilities for the expected future tax effects attributable to temporary differences between the financial statement and tax return bases of assets and liabilities based on enacted tax rates and other provisions of the tax law. The effect of a change in tax laws or rates on deferred tax assets and liabilities is recognized in income in the period in which such change is enacted. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that all or some portion of the deferred tax assets will not be realized. Deferred tax positions are not established for adjustments arising from foreign operations whose earnings are considered to be permanently reinvested.

(dollars in millions)

The Company's effective tax rate on continuing operations differs from the U.S. Federal statutory rate of 35% principally due to tax-exempt investment income. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

Balance as of December 31, 2016	$99
Additions for tax positions in current year	2
Additions for tax positions of prior years	14
Reductions for tax positions of prior years	(4)
Translation	1
Balance as of March 31, 2017	$112

Included in the tabular roll forward of unrecognized tax benefits is interest and penalties in the amount of $6 and $6 as of March 31, 2017 and December 31, 2016, respectively.

Included in the balance at March 31, 2017, is $35 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. For the three months ended March 31, 2017 and 2016, the Company recognized $0 and $1 of interest and penalties in each period. The Company had $6 and $6 of interest and penalties accrued as of March 31, 2017 and December 31, 2016, respectively.

The IRS has completed its review of the Company's United States Federal income tax returns through the 2009 tax year and is currently reviewing income tax returns for the 2010 through 2014 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.

The Company believes that the range of reasonably possible changes to the balance of unrecognized tax benefits could decrease by $0 to $20 within the next twelve months as a result of potential settlements with the IRS for prior years.

(8) BENEFIT PLANS

The net benefit costs for the three months ended March 31, 2017 and 2016, include the following components:

Three months ended March 31,	**Pension Benefits**		**Supplemental Pension Benefits [1]**		**Postretirement Benefits**	
	2017	**2016**	**2017**	**2016**	**2017**	**2016**
Components of net periodic benefit costs:						
Service costs	$38	$33	$1	$1	$5	$4
Interest costs	71	77	4	4	9	9
Expected return on plan assets	(125)	(115)	-	-	-	-
Amortization of unrecognized:						
Net loss	45	38	6	5	1	-
Prior service cost	(7)	(1)	(1)	-	(3)	(3)
Net periodic benefit costs	$22	$32	$10	$10	$12	$10

[1] The Company sponsors non-qualified supplemental pension plans to restore to selected highly compensated employees the pension benefits to which they would be entitled under the Company's U.S. tax qualified, defined benefit pension plan had it not been for limits imposed by the Internal Revenue Code. The supplemental plans are unfunded.

Effective January 1, 2016, service cost is calculated by discounting the future cash flows attributable to the current year of service using spot rates specifically applicable to the timing of the cash flows. Interest cost is determined by multiplying each benefit obligation cash flow by the spot rate applicable to that timing of the cash flow.

The Company has contributed $401 to the qualified plans as of March 31, 2017 and expects to additionally contribute approximately $17.

(9) FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the price that would be received to sell an asset or would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Company primarily uses the market approach, which generally utilizes market transaction data for identical or similar instruments.

The hierarchy level assigned to each security in the Company's available for sale portfolio is based on the Company's assessment of the transparency and reliability of the inputs used in the valuation of each instrument at the measurement date. The highest priority is given to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). Securities are classified based on the lowest level of input that is significant to the fair value measurement. The Company recognizes transfers between levels at the end of each reporting period. The three hierarchy levels are defined as follows:

- Level 1 — Valuations based on unadjusted quoted market prices in active markets for identical assets or liabilities that the Company has the ability to access.
- Level 2 — Valuations based on observable inputs (other than Level 1 prices), such as quoted prices for similar assets or liabilities at the measurement date, quoted prices in markets that are not active, or other inputs that are observable, either directly or indirectly.
- Level 3 — Valuations based on inputs that are unobservable and significant to the overall fair value measurement and involve management judgment. The unobservable inputs reflect the Company's estimates of the assumptions that market participants would use in valuing the assets and liabilities.

The availability of observable inputs can vary from financial instrument to financial instrument and is affected by a wide variety of factors, including, for example, the type of financial instrument, whether the financial instrument is new and not yet established in the marketplace, and other characteristics particular to the financial instrument. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires significantly more judgment. Accordingly, the degree of judgment exercised by management in determining fair value is greatest for instruments categorized in Level 3.

The Company is responsible for the determination of fair value and the supporting assumptions and methodologies. The Company gains assurance on the overall reasonableness and consistent application of valuation methodologies and inputs and compliance with accounting standards through the execution of various processes and controls designed to ensure that the Company's assets and liabilities are appropriately valued. For fair values received from third parties or internally estimated, the Company's processes are designed to determine that the valuation methodologies and inputs are appropriate and consistently applied, the assumptions are reasonable and consistent with the objective of determining fair value, and the fair values are accurately recorded. For example, on a continuing basis, the Company assesses the reasonableness of individual fair values that have stale security prices or that exceed certain thresholds as compared to previous fair values received from valuation service providers or brokers or derived from internal models. The Company performs procedures to understand and assess the methodologies, processes and controls of valuation service providers. In addition, the Company may validate the reasonableness of fair values by comparing information obtained from valuation service providers or brokers to other third party valuation sources for selected securities.

The Company used the following methods and assumptions in estimating the fair value of its financial instruments as well as the general classification of such financial instruments pursuant to the above fair value hierarchy:

Fixed Maturities
At each valuation date, the Company uses various valuation techniques to estimate the fair value of its fixed maturities portfolio. The primary method for valuing the Company's securities is through independent third-party valuation service providers. For positions where valuations are not available from independent third-party valuation service providers, the Company utilizes broker quotes and internal pricing methods to determine fair values. The Company obtains a single non-binding price quote from a broker familiar with the security who, similar to the Company's valuation service providers, may consider transactions or activity in similar securities, as applicable, among other information. The brokers providing price quotes are generally from the brokerage divisions of leading financial institutions with market making, underwriting and distribution expertise regarding the security subject to valuation. The evaluation and prioritization of these valuation sources is systematic and predetermined resulting in a single quote or price for each financial instrument. The following describes the techniques generally used to determine the fair value of the Company's fixed maturities by asset class:

U.S. Government and Agency Securities
U.S. government and agency securities consist primarily of bonds issued by the U.S. Treasury and mortgage pass-through agencies such as the Federal Home Loan Bank, the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation. As the fair values of the Company's U.S. Treasury securities are based on active markets and unadjusted market prices, they are classified within Level 1. The fair value of U.S. government agency securities is generally determined using observable market inputs that include quoted

prices for identical or similar assets in markets that are not active, benchmark yields, reported trades, bids, offers and credit spreads. Accordingly, the fair value of U.S. government agency securities is primarily classified within Level 2.

Mortgage-Backed Securities

The Company's portfolio of residential and commercial MBS is originated by both agencies and non-agencies, the majority of which are pass-through securities issued by U.S. government agencies. The fair value of MBS is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active, benchmark yields, contractual cash flows, prepayment speeds, collateral performance and credit spreads. Accordingly, the fair value of MBS is primarily classified within Level 2.

Asset-Backed Securities

ABS include mostly investment-grade bonds backed by pools of loans with a variety of underlying collateral, including automobile loan receivables, credit card receivables, and collateralized loan obligation securities originated by a variety of financial institutions. The fair value of ABS is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active, benchmark yields, contractual cash flows, prepayment speeds, collateral performance and credit spreads. Accordingly, the fair value of ABS is primarily classified within Level 2.

Municipal Securities

The Company's municipal portfolio is comprised of bonds issued by U.S. domiciled state and municipal entities. The fair value of municipal securities is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active, benchmark yields, binding broker quotes, issuer ratings, reported trades and credit spreads. Accordingly, the fair value of municipal securities is primarily classified within Level 2.

Corporate Debt and Other Securities

Corporate debt securities consist primarily of investment-grade debt of a wide variety of corporate issuers and industries. The fair value of corporate and other securities is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active, benchmark yields, new issuances, issuer ratings, reported trades of identical or comparable securities, bids, offers and credit spreads. Accordingly, the fair value of corporate and other securities is primarily classified within Level 2. In the event third-party vendor valuation is not available, prices are determined using non-binding price quotes from a broker familiar with the security. In this instance, the valuation inputs are generally unobservable and the fair value is classified within Level 3.

Foreign Government Securities

Foreign government securities include bonds issued or guaranteed by foreign governments. The fair value of foreign government securities is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active, benchmark yields, binding broker quotes, issuer ratings, reported trades of identical or comparable securities and credit spreads. Accordingly, the fair value of foreign government securities is primarily classified within Level 2. In the event third-party vendor valuation is not available, prices are determined using non-binding price quotes from a broker familiar with the security. In this instance, the valuation inputs are generally unobservable and the fair value is classified within Level 3.

Equity Securities

Equity securities include common and preferred stocks. Common stocks with fair values based on quoted market prices in active markets are classified within Level 1. Common stocks with fair values determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active are classified within Level 2. The fair value of preferred stock is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active. Accordingly, the fair value of preferred stock is primarily classified within Level 2.

Short-Term Investments

The fair value of short-term investments is generally determined using observable market inputs that include quoted prices for identical or similar assets in markets that are not active, benchmark yields, new issuances, issuer ratings, reported trades of identical or comparable securities, bids, offers and credit spreads. Accordingly, the fair value of short-term investments is primarily classified within Level 2 of the fair value hierarchy.

Other Investments

Other investments include primarily foreign cash deposits and equity investments in privately held businesses. Cash deposits are primarily valued using quoted prices for similar instruments in active markets; these assets are categorized within Level 2 of the fair value hierarchy. Equity investments in privately held businesses are valued using internal management estimates; they are categorized within Level 3 of the hierarchy. Loans, limited partnership and other equity method investments, which represent the remainder of the other investment balance on the accompanying consolidated balance sheet are not subject to these disclosures and therefore are excluded from the table in this note.

Separate Account Assets

Separate account assets, which primarily consist of other limited partnerships and equity securities, are measured based on the methodologies discussed above. The activity in separate account assets is offset by an equal amount for separate account liabilities, which results in a net zero impact for the Company. Separate account assets within Level 3 include other limited partnership interests. Other limited partnership interests are valued giving consideration to the value of the underlying holdings of the partnerships.

Other Assets and Other Liabilities

Other assets primarily consist of fixed maturities, short-term investments, and equity securities of captive companies sponsored by the Company. These assets are measured based on the methodology for individual securities as discussed above.

Additionally, other assets and other liabilities classified within Level 2 represent the Company's derivatives which can be exchange-traded or traded over-the-counter ("OTC"). OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. When models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in the instrument, as well as the availability of pricing information in the market. The Company generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be corroborated by observable market data by correlation or other means, and model selection does not involve significant management judgment.

Life Insurance Obligations

Life insurance obligations include certain variable annuity contracts that provide guaranteed minimum income benefits. These benefits are accounted for as embedded derivatives and are bifurcated from the host contract and carried at fair value. The fair value of these embedded derivatives are computed on a recurring basis using assumptions predominately classified as Level 3 (significant unobservable) inputs. While some inputs are observable in the market, such as risk free rates, volatility and historical equity returns, the underlying future policyholder behavior inputs are highly unobservable. The significant policyholder behavior assumptions include lapse and the underlying annuitization rate.

(dollars in millions)

The following tables summarize the Company's assets and liabilities that are measured at fair value on a recurring basis as of March 31, 2017 and December 31, 2016:

	As of March 31, 2017			
Assets, at Fair Value	**Level 1**	**Level 2**	**Level 3**	**Total**
U.S. government and agency securities	$2,473	$649	$ -	$3,122
Residential MBS	-	6,345	-	6,345
Commercial MBS	-	1,663	44	1,707
Other MBS and ABS	-	2,756	19	2,775
U.S. state and municipal	-	13,683	180	13,863
Corporate and other	-	31,947	100	32,047
Foreign government securities	-	5,045	-	5,045
Total fixed maturities, available for sale	2,473	62,088	343	64,904
Common stock	2,313	-	39	2,352
Preferred stock	-	349	4	353
Total equity securities, available for sale	2,313	349	43	2,705
Short-term investments	-	629	6	635
Other investments	-	65	537	602
Separate account assets	34	-	76	110
Other assets	-	4	20	24
Total assets	$4,820	$63,135	$1,025	$68,980
Liabilities, at Fair Value				
Life insurance obligations	$-	$-	$(133)	$(133)
Other liabilities	-	(35)	-	(35)
Total liabilities	$-	$(35)	$(133)	$(168)

	As of December 31, 2016			
Assets, at Fair Value	**Level 1**	**Level 2**	**Level 3**	**Total**
U.S. government and agency securities	$2,562	$668	$ -	$3,230
Residential MBS	-	6,651	-	6,651
Commercial MBS	-	1,634	44	1,678
Other MBS and ABS	-	2,932	48	2,980
U.S. state and municipal	-	14,102	180	14,282
Corporate and other	-	30,725	100	30,825
Foreign government securities	-	5,054	-	5,054
Total fixed maturities, available for sale	2,562	61,766	372	64,700
Common stock	2,201	-	38	2,239
Preferred stock	-	333	4	337
Total equity securities, available for sale	2,201	333	42	2,576
Short-term investments	5	1,137	5	1,147
Other investments	-	77	526	603
Separate account assets	39	-	65	104
Other assets	-	1	21	22
Total assets	$4,807	$63,314	$1,031	$69,152
Liabilities, at Fair Value				
Life insurance obligations	$ -	$ -	$(136)	$(136)
Other liabilities	-	(46)	(1)	(47)
Total liabilities	$ -	$(46)	$(137)	$(183)

(dollars in millions)

The Company did not have significant transfers between Levels 1 and 2 for the three months ended March 31, 2017.

The following tables summarize the fair values of assets on a recurring basis classified as Level 3 within the fair value hierarchy:

	Balance January 1, 2017	Net Realized Gains (Losses)	Net Unrealized Gains (Losses)	Purchases	Settlements	Sales and Maturities	Transfer in to Level 3	Transfer out of Level 3	Balance March 31, 2017
Assets, at Fair Value									
U.S. government and agency securities	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Residential MBS	-	-	-	-	-	-	-	-	-
Commercial MBS	44	-	-	-	-	-	-	-	44
Other MBS and ABS	48	-	1	-	-	-	-	(30)	19
U.S. state and municipal	180	-	1	-	-	(1)	-	-	180
Corporate and other	100	-	-	1	-	(1)	-	-	100
Foreign government securities	-	-	-	-	-	-	-	-	-
Total fixed maturities	372	-	2	1	-	(2)	-	(30)	343
Common stock	38	-	-	1	-	-	-	-	39
Preferred stock	4	-	-	-	-	-	-	-	4
Total equity securities	42	-	-	1	-	-	-	-	43
Short-term investments	5	-	1	-	-	-	-	-	6
Other investments	526	-	11	-	-	-	-	-	537
Separate account assets	65	-	-	-	-	-	11	-	76
Other assets	21	-	-	(1)	-	-	-	-	20
Total assets	$1,031	$-	$14	$1	$-	$(2)	$11	$(30)	$1,025
Liabilities, at Fair Value									
Life insurance obligations	$(136)	$-	$-	$3	$-	$-	$-	$-	$(133)
Other Liabilities	(1)	-	1	-	-	-	-	-	-
Total liabilities	$(137)	$-	$1	$3	$-	$-	$-	$-	$(133)

	Balance January 1, 2016	Net Realized Gains (Losses)	Net Unrealized (Losses) Gains	Purchases	Settlements	Sales and Maturities	Transfer in to Level 3	Transfer out of Level 3	Balance December 31, 2016
Assets, at Fair Value									
U.S. government and agency securities	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Residential MBS	1	-	-	4	-	-	-	(5)	-
Commercial MBS	75	-	-	17	-	-	1	(49)	44
Other MBS and ABS	80	-	(1)	-	-	(1)	29	(59)	48
U.S. state and municipal	244	-	5	152	-	(25)	8	(204)	180
Corporate and other	235	3	1	37	-	(144)	1	(33)	100
Foreign government securities	10	-	-	-	-	(1)	-	(9)	-
Total fixed maturities	645	3	5	210	-	(171)	39	(359)	372
Common stock	42	-	1	-	-	(5)	-	-	38
Preferred stock	4	-	-	-	-	-	-	-	4
Total equity securities	46	-	1	-	-	(5)	-	-	42
Short-term investments	-	-	-	6	-	-	-	(1)	5
Other investments	479	-	28	25	-	(6)	-	-	526
Separate account assets	64	5	-	-	-	(4)	-	-	65
Other assets	25	(1)	-	(3)	-	-	-	-	21
Total assets	$1,259	$7	$34	$238	$ -	$(186)	$39	$(360)	$1,031
Liabilities, at Fair Value									
Life insurance obligations	$(154)	$-	$ -	$18	$ -	$ -	$ -	$ -	$(136)
Other liabilities	-	-	(1)	-	-	-	-	-	(1)
Total liabilities	$(154)	$-	$ (1)	$18	$ -	$ -	$ -	$ -	$(137)

Transfers into and out of Level 3 were primarily due to changes in the observability of pricing inputs.

There were no material unrealized gains (losses) for the period included in earnings attributable to the fair value relating to assets and liabilities classified as Level 3 that are still held as of March 31, 2017.

The Company's assets measured on a non-recurring basis are primarily related to direct investments in oil and gas production and real estate. These assets are measured on a non-recurring basis at the time of impairment and are not included in the tables presented above. The Company's assets classified as Level 3 were $10 as of March 31, 2017.

For the three months ended March 31, 2017, there were impairments recognized of $31 for items measured at fair value on a nonrecurring basis.

The Company has not applied ASC 820, *Fair Value Measurements and Disclosures*, to non-financial assets and liabilities.

(10) COMMITMENTS AND CONTINGENT LIABILITIES

Various lawsuits against the Company have arisen in the normal course of business. Contingent liabilities arising from litigation, income taxes, and other matters are not considered material in relation to the financial position of the Company.

As of March 31, 2017, the Company had unfunded commitments in traditional private equity partnerships, natural resources, real estate, and other of $1,682, $566 (all of which is related to energy investments), $597, and $477, respectively.

As of March 31, 2017, the Company had commitments to purchase various residential MBS at a cost and fair value of $353 and $356, respectively.

(11) SUBSEQUENT EVENTS

On May 1, 2017, the Company acquired Ironshore Inc. for approximately $2,900 subject to standard post-closing adjustments. Transaction related costs primarily consist of non-recurring banking, legal, tax, and accounting expenses and are reflected on the consolidated statements of income separately. Concurrent with the acquisition, the Company will combine its existing Liberty International Underwriters' U.S. business and Ironshore's U.S. specialty lines business under the Ironshore brand. On May 2, 2017, Ironshore exercised its option to redeem in full its outstanding $250 Ironshore Holdings (US) Inc. 8.5% Senior Notes maturing in 2020 in accordance with the contractual make whole provisions.

On April 17, 2017, the Company completed the acquisition of TRU Services, LLC, specializing in providing medical stop loss products to mid and large-size medical plan sponsors. The transaction is not material to the Company.

Management has assessed material subsequent events through May 4, 2017, the date the financial statements were available to be issued.