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

Year Ended December 31, 2011

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 and twelve months ended December 31, 2011 and 2010. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's 2011 Audited Consolidated Financial Statements and Fourth Quarter 2011 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.

Index

	Page
Cautionary Statement Regarding Forward Looking Statements	3
Executive Summary	4
Consolidated Results of Operations	6
Review of Financial Results by Business Unit	
Liberty Mutual Agency Corporation	14
International	19
Personal Markets	23
Commercial Markets	26
Corporate and Other	30
Investments	33
Liquidity and Capital Resources	41
Critical Accounting Policies	46
About the Company	53

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 2011 Audited Consolidated Financial Statements.

Three Months Ended December 31, 2011 - Consolidated Results of Operations

- Revenues for the three months ended December 31, 2011 were $8.963 billion, an increase of $413 million or 4.8% over the same period in 2010.
- Net written premium for the three months ended December 31, 2011 was $7.722 billion, an increase of $743 million or 10.6% over the same period in 2010.
- Pre-tax operating income before LP and LLC income for the three months ended December 31, 2011 was $155 million, a decrease of $360 million or 69.9% from the same period in 2010.
- Pre-tax operating income for the three months ended December 31, 2011 was $262 million, a decrease of $417 million or 61.4% from the same period in 2010.
- Net income attributable to LMHC for the three months ended December 31, 2011 was $284 million, a decrease of $292 million or 50.7% from the same period in 2010.
- Cash flows from operations for the three months ended December 31, 2011 were $621 million, a decrease of $386 million or 38.3% from the same period in 2010.
- The consolidated combined ratio before catastrophes[1] , net incurred losses attributable to prior years[2] and current accident year re-estimation[3] for the three months ended December 31, 2011 was 98.3%, an increase of 1.0 point over the same period in 2010. Including the impact of catastrophes, net incurred losses attributable to prior years and current accident year re-estimation, the Company's combined ratio for the three months ended December 31, 2011 increased 5.0 points to 104.2%.

Twelve Months Ended December 31, 2011 - Consolidated Results of Operations

- Revenues for the twelve months ended December 31, 2011 were $34.671 billion, an increase of $1.478 billion or 4.5% over the same period in 2010.
- Net written premium for the twelve months ended December 31, 2011 was $31.183 billion, an increase of $1.992 billion or 6.8% over the same period in 2010.
- Pre-tax operating loss before LP and LLC income for the twelve months ended December 31, 2011 was $334 million versus $1.521 billion of pre-tax operating income before LP and LLC income in the same period in 2010.

---

[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 2010 Chile and New Zealand earthquakes, 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.

[3] Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.

- Pre-tax operating income for the twelve months ended December 31, 2011 was $249 million, a decrease of $1.670 billion or 87.0% from the same period in 2010.

- Net income attributable to LMHC for the twelve months ended December 31, 2011 was $365 million, a decrease of $1.313 billion or 78.2% from the same period in 2010.

- Cash flows from operations for the twelve months ended December 31, 2011 were $2.101 billion, a decrease of $660 million or 23.9% from the same period in 2010.

- The consolidated combined ratio before catastrophes and net incurred losses attributable to prior years for the twelve months ended December 31, 2011 was 97.5%, a decrease of 0.1 points from the same period in 2010. Including the impact of catastrophes and net incurred losses attributable to prior years, the Company's combined ratio for the twelve months ended December 31, 2011 increased 6.2 points to 107.4%.

Financial Condition as of December 31, 2011

- Total assets were $117.131 billion as of December 31, 2011, an increase of $4.781 billion over December 31, 2010.

- Total equity was $17.864 billion as of December 31, 2011, an increase of $880 million over December 31, 2010.

Subsequent Events

- On January 11, 2012, Liberty Mutual Fire Insurance Company ("LMFIC") became a member of the Federal Home Loan Bank of Chicago. This membership provides the Company with access to a secured asset-based borrowing with loan maturities of up to 30 years. To date, no funds have been borrowed.

- On January 20, 2012, Liberty Mutual Group Inc. ("LMGI") entered into interest rate swap transactions having a notional amount of $300 million with respect to LMGI's $300 million 7% 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.

- On March 5, 2012, the Company entered into two multi-year property catastrophe reinsurance agreements with Mystic Re III Ltd. ("Mystic III"), a Cayman Islands domiciled insurer, 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.

CONSOLIDATED RESULTS OF OPERATIONS

The Company has identified consolidated pre-tax operating income (loss) and pre-tax operating income (loss) before LP and LLC income (loss) as non-GAAP financial measures. Pre-tax operating income (loss) is defined by the Company as pre-tax income excluding net realized gains (losses), loss on extinguishment of debt, extraordinary items, discontinued operations, integration and other acquisition related costs and cumulative effects of changes in accounting principles. Pre-tax operating income (loss) before LP and LLC income (loss) is defined as pre-tax operating income (loss) excluding LP and LLC results recognized on the equity method. Pre-tax operating income (loss) before LP and LLC income (loss) and pre-tax operating income (loss) 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 (losses) 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 "net written premium" 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 net written premium 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.

Effective January 1, 2010, the Company's Venezuela operations began applying hyper-inflationary accounting, utilizing the U.S. dollar as the functional currency, which had no impact on total policyholders' equity at January 1, 2010. However, on January 8, 2010, the Venezuela government devalued its currency, announcing that the fixed official exchange rate would be changed to a dual exchange rate system. This dual exchange rate system for the fixed official exchange rate included a 2.60 Bolivar Fuerte (BsF) rate to 1 U.S. dollar for food and other items as mandated by the Venezuela government, and a 4.30 BsF to 1 U.S. dollar rate for all other items.

On December 30, 2010, the Venezuela government announced the elimination of the 2.60 BsF to 1 U.S. dollar preferential exchange rate effective January 1, 2011, which was applicable to imports of food, medicine, other essential items and certain investments. The elimination of the preferential exchange rate resulted in an increase of $132 million to total policyholders' equity in the first quarter of 2011.

Effective in the third quarter of 2010, for financial reporting purposes, Liberty Mutual Agency Corporation ("LMAC") became a Strategic Business Unit ("SBU") of the Company replacing the former Agency Markets SBU. The financial results of LMAC differ from Agency Markets' results principally due to LMAC maintaining a dedicated investment portfolio and certain expenses incurred that are specific to LMAC. As such, results of LMAC are not directly comparable to the previously reported financial information for Agency Markets.

Overview – Consolidated

Consolidated net written premium ("NWP") by significant line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Private passenger automobile	$2,788	$2,585	7.9%	$10,848	$10,231	6.0%
Workers compensation	868	734	18.3	3,715	3,698	0.5
Homeowners	800	721	11.0	3,229	2,928	10.3
Commercial multiple peril / fire	603	551	9.4	2,513	2,385	5.4
International local businesses (excluding private passenger automobile)	569	494	15.2	2,139	1,800	18.8
Commercial automobile	350	354	(1.1)	1,478	1,540	(4.0)
Lloyd's Syndicate 4472	272	255	6.7	1,456	1,200	21.3
General liability	339	260	30.4	1,317	1,194	10.3
LIU[1] third party	224	203	10.3	852	686	24.2
Group disability and life	192	178	7.9	787	693	13.6
Surety	172	165	4.2	749	731	2.5
LIU inland marine program	106	109	(2.8)	405	606	(33.2)
LIU first party	93	80	16.3	369	311	18.6
Individual life	124	72	72.2	365	266	37.2
Other[2] (including AVR)	222	218	1.8	961	922	4.2
Total NWP[3]	$7,722	$6,979	10.6%	$31,183	$29,191	6.8%

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

Consolidated net written premium by SBU was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
LMAC	$2,655	$2,548	4.2%	$10,634	$10,549	0.8%
International	2,106	1,914	10.0	8,209	7,244	13.3
Personal Markets	1,799	1,617	11.3	7,378	6,776	8.9
Commercial Markets	1,260	1,098	14.8	5,572	5,183	7.5
Corporate and Other	(98)	(198)	(50.5)	(610)	(561)	8.7
Total NWP	$7,722	$6,979	10.6%	$31,183	$29,191	6.8%
Foreign exchange effect on growth			(0.5%)			0.4 %
NWP growth excluding foreign exchange			11.1%			6.4%

Major drivers of net written premium growth were as follows:

$ in Millions	Three Months Ended December 31, 2011	2010	$ Change	Points Attribution	Twelve Months Ended December 31, 2011	2010	$ Change	Points Attribution
Total NWP	$7,722	$6,979	$743	10.6	$31,183	$29,191	$1,992	6.8
Components of Growth:								
International local businesses (excluding foreign exchange)	1,469	1,264	205	2.9	5,172	4,523	649	2.2
-Domestic homeowners	973	878	95	1.4	3,926	3,565	361	1.2
-Homeowners quota share	(173)	(157)	(16)	(0.2)	(697)	(637)	(60)	(0.2)
Total Homeowners	800	721	79	1.2	3,229	2,928	301	1.0
Lloyd's Syndicate 4472	272	255	17	0.2	1,456	1,200	256	0.9
Domestic personal auto	1,926	1,815	111	1.6	7,714	7,508	206	0.7
Foreign exchange	(37)	-	(37)	(0.5)	129	-	129	0.4
Group disability and life	192	178	14	0.2	787	693	94	0.3
Individual life	124	72	52	0.7	365	266	99	0.3
Surety	172	165	7	0.1	749	731	18	0.1
Other commercial lines	2,804	2,509	295	4.2	11,582	11,342	240	0.9
Total NWP	$7,722	$6,979	$743	10.6	$31,183	$29,191	$1,992	6.8

Consolidated net written premium by geographic distribution channels was as follows:

$ in Millions	Three Months Ended December 31, 2011	2010	Change	Twelve Months Ended December 31, 2011	2010	Change
U.S.	$5,836	$5,292	10.3%	$23,887	$22,990	3.9%
International[1]	1,886	1,687	11.8	7,296	6,201	17.7
Total NWP	$7,722	$6,979	10.6%	$31,183	$29,191	6.8%

1 Excludes domestically written business in the International SBU.

Net written premium for the three and twelve months ended December 31, 2011 was $7.722 billion and $31.183 billion, respectively, increases of $743 million and $1.992 billion over the same periods in 2010. Significant changes by major line of business include:

- Private passenger automobile net written premium increased $203 million and $617 million in the quarter and year, respectively. The increases in both periods primarily reflect growth of policies in-force and rate increases in Personal Markets, organic growth in International's local businesses, primarily in Latin America, and higher rate, retention and new business in LMAC. The increase in the year was partially offset by the timing of LMAC renewal premium due to the introduction of an annual private passenger automobile product in the second half of 2010 which resulted in formerly six month term policies that previously renewed in the first six months of the year now having an additional twelve months of premium recorded at renewal and reverting back to annual premium in 2011. The increases reflect 6.2% in unit growth as compared to December 31, 2010.
- Workers compensation net written premium increased $134 million and $17 million in the quarter and year, respectively. The increases in both periods were primarily driven by an increase in audit premium as well as higher rates and exposures. The increase in the year also reflects a significant construction account with multi-year exposures (in Commercial Markets), substantially offset by the Company's workers compensation "booked as billed" adjustment (in Corporate and Other). The quarter was also impacted by the "booked as billed" adjustment.

- Homeowners net written premium increased $79 million and $301 million in the quarter and year, respectively. The increases in both periods were primarily driven by Personal Markets' and LMAC's growth in homeowners policies in-force and rate increases.
- International local businesses net written premium (excluding private passenger automobile) increased $75 million and $339 million in the quarter and year, respectively. The increases in both periods were primarily driven by organic growth in Latin America, led by Venezuela (primarily due to the impact of inflation), and to a lesser extent, Asia, led by China. The increases also reflect the acquisition of Quinn Insurance Limited ("QIL") in November 2011.
- Lloyd's Syndicate 4472 net written premium increased $17 million and $256 million in the quarter and year, respectively. The increases are primarily due to new programs that diversify our risk, such as agriculture, direct auto, trade credit, and marine; and also due to reinstatement premiums from contracts that experienced losses.
- General liability net written premium increased $79 million and $123 million in the quarter and year, respectively. The increases in both periods reflect a large account written in Commercial Markets.
- LIU third party net written premium increased $21 million and $166 million in the quarter and year, respectively. The increases primarily reflect new business in specialty casualty lines.
- Group disability and life net written premium increased $14 million and $94 million in the quarter and year, respectively. The increases in both periods reflect higher retention and new business writings. The year increase also reflects a large disability account written in the first quarter.
- LIU inland marine program net written premium decreased $3 million and $201 million in the quarter and year, respectively. The decrease in the year reflects higher ceded premium due to a change in a reinsurance program resulting in less net premium retained.
- LIU first party net written premium increased $13 million and $58 million in the quarter and year, respectively. The increases in both periods reflect U.S. oil and gas business with higher renewals from increased participation and higher values, the expansion of UK regional commercial business and an increase in energy and property business in the Asia Pacific region due to rate increases related to catastrophe losses experienced in 2011.
- Individual life net written premium increased $52 million and $99 million in the quarter and year, respectively. The increases were primarily driven by strong structured settlement sales in the second half of the year.

More detailed explanations of the changes in net written premium by line of business are included in the related discussion of financial results for each 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 December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Revenues	$8,963	$8,550	4.8%	$34,671	$33,193	4.5%
Pre-tax operating income (“PTOI”) before catastrophes, net incurred losses attributable to prior years, Venezuela devaluation, current accident year re-estimation and LP and LLC income	$598	$574	4.2%	$2,481	$2,234	11.1%
Catastrophes[1]	(234)	(198)	18.2	(2,681)	(1,257)	113.3
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	(10)	(4)	150.0	(351)	(9)	NM
- All other[3]	(78)	150	NM	217	325	(33.2)
Venezuela devaluation	-	25	(100.0)	-	228	(100.0)
Current accident year re-estimation[4]	(121)	(32)	NM	-	-	-
Pre-tax operating income (loss) before LP and LLC income	155	515	(69.9)	(334)	1,521	NM
LP and LLC income[5]	107	164	(34.8)	583	398	46.5
PTOI	262	679	(61.4)	249	1,919	(87.0)
Net realized (losses) gains	(10)	110	NM	158	402	(60.7)
Loss on extinguishment of debt	(33)	-	NM	(110)	-	NM
Pre-tax income	219	789	(72.2)	297	2,321	(87.2)
Income tax benefit (expense)	63	(213)	NM	71	(637)	NM
Consolidated net income	282	576	(51.0)	368	1,684	(78.1)
Less: Net (loss) income attributable to non-controlling interests	(2)	-	NM	3	6	(50.0)
Net income attributable to LMHC	$284	$576	(50.7%)	$365	$1,678	(78.2%)
Cash flows from operations	$621	$1,007	(38.3%)	$2,101	$2,761	(23.9%)

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 2010 Chile and New Zealand earthquakes, 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 twelve months ended December 31, 2011 include $294 million of strengthening of asbestos related reserves in connection with a ground-up reserve study.

3 Net of earned premium attributable to prior years of ($42) million and ($26) million for the three and twelve months ended December 31, 2011 and $39 million and ($64) million for the same periods in 2010. Net of amortization of deferred gains on retroactive reinsurance of $5 million and $134 million for the three and twelve months ended December 31, 2011 and $1 million and $54 million for the same periods in 2010. The twelve months ended December 31, 2011 reflect a gain on commutation of two retroactive reinsurance contracts during the first quarter.

4 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.

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

NM = Not Meaningful

Pre-tax operating income for the three and twelve months ended December 31, 2011 was $262 million and $249 million, respectively, decreases of $417 million and $1.670 billion from the same periods in 2010. The decreases in both periods are primarily due to higher catastrophe losses and unfavorable net incurred losses attributable to prior years recorded in the fourth quarter of 2011 compared to favorable development in 2010, partially offset by premium growth. The quarter was also impacted by current accident year re-estimation. The year also reflects increases in asbestos and environmental reserves and a gain on Venezuela devaluation in 2010 that did not recur, partially offset by LP and LLC income due to improved market valuations and a gain on the commutation of two workers compensation retroactive reinsurance agreements.

Revenues for the three and twelve months ended December 31, 2011 were $8.963 billion and $34.671 billion, respectively, increases of $413 million and $1.478 billion over the same periods in 2010. 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 and twelve months ended December 31, 2011 was $7.887 billion and $30.119 billion, respectively, increases of $544 million and $1.420 billion over the same periods in 2010. The increases in both periods primarily reflect 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 to a lesser extent, Asia, partially offset by the impact of the Venezuela devaluation in 2010. The increase in the year also reflects a decrease in the estimate of prior year earned premium on loss sensitive business recorded in the twelve months ended December 31, 2010 and a foreign exchange gain excluding the impact of Venezuela.

Net investment income for the three and twelve months ended December 31, 2011 was $853 million and $3.523 billion, respectively, a decrease of $44 million and increase of $195 million versus the same periods in 2010. The changes in the quarter and the year compared to prior year primarily reflect valuation changes in LP and LLC investments.

Net realized (losses) gains for the three and twelve months ended December 31, 2011 were ($10) million and $158 million, respectively, decreases of $120 million and $244 million from the same periods in 2010. The decreases primarily reflect a net foreign exchange loss recognized in 2011 on Venezuela and Argentina securities, combined with sales undertaken during 2010 in connection with the shift in the Company's tactical allocation that did not recur in 2011. The decreases were partially offset by gains recognized in connection with the prior sale of certain Commercial Markets policy renewal rights and gains associated with the Company's investments in the energy sector.

Fee and other revenues for the three and twelve months ended December 31, 2011 were $233 million and $871 million, respectively, increases of $33 million and $107 million over the same periods in 2010. The increases in both periods primarily reflect higher oil and gas revenues in Corporate and Other due to increased production and premium financing revenues due to business growth in International.

Claims, benefits and expenses for the three and twelve months ended December 31, 2011 were $8.711 billion and $34.264 billion, respectively, increases of $950 million and $3.392 billion over the same periods in 2010. The increases in both periods reflect higher catastrophe losses and increases in losses and expenses consistent with business growth. Impacting the quarter were unfavorable incurred losses attributable to prior years compared to favorable development in 2010 and a re-estimation of current accident year losses in Commercial Markets and LMAC for commercial liability lines. The increase in the year also reflects increases in asbestos and environmental reserves and less favorable incurred losses attributable to prior years excluding asbestos and environmental reserves. The increase in the year was partially offset by a foreign exchange loss as a result of the Venezuela devaluation in 2010 that did not recur and a gain on the commutation of two workers compensation retroactive reinsurance agreements.

Income tax benefit for the three and twelve months ended December 31, 2011 was $63 million and $71 million, respectively, decreases of $276 million and $708 million, respectively, from the same periods in 2010. The Company's effective tax rate for the three and twelve months ended December 31, 2011 was (29%) and (24%), compared to 27% for both periods in 2010. The decrease in effective tax rate was primarily due to lower pre-tax income in 2011 and a 2010 one time charge of $55 million related to the federal health care legislation which eliminated the tax benefit associated with Medicare Part D subsidies. The Company's effective tax rate differs from the Federal statutory rate of 35% principally due to tax-exempt investment income and foreign taxes.

Net income for the three and twelve months ended December 31, 2011, was $284 million and $365 million, respectively, decreases of $292 million and $1.313 billion from the same periods in 2010.

Cash flows from operations for the three and twelve months ended December 31, 2011 were $621 million and $2.101 billion, respectively, decreases of $386 million and $660 million from the same periods in 2010. The decreases in both periods reflect higher catastrophe paid losses partially offset by premium collections. The year also reflects increased ceded premium payments and higher federal tax payments due to a refund in 2010 that did not recur in 2011, partially offset by the settlement of a large asbestos claim that was paid in 2010 that did not recur in 2011.

	Three Months Ended December 31,			Twelve Months Ended December 31,		
CONSOLIDATED	**2011**	**2010[1]**	**Change (Points)**	**2011**	**2010[1]**	**Change (Points)**
Combined ratio before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation						
Claims and claim adjustment expense ratio	70.0%	68.3%	1.7	68.9%	68.9%	-
Underwriting expense ratio	28.1	28.9	(0.8)	28.4	28.5	(0.1)
Dividend ratio	0.2	0.1	0.1	0.2	0.2	-
Subtotal	98.3	97.3	1.0	97.5	97.6	(0.1)
Catastrophes[2]	3.1	2.8	0.3	9.3	4.6	4.7
Net incurred losses attributable to prior years:						
- Asbestos & environmental	0.1	0.8	(0.7)	1.3	0.2	1.1
- All other	1.1	(2.2)	3.3	(0.7)	(1.2)	0.5
Current accident year re-estimation[3]	1.6	0.5	1.1	-	-	-
Total combined ratio[4]	104.2%	99.2%	5.0	107.4%	101.2%	6.2

1 2010 combined ratio has been adjusted to exclude the impact of the Venezuela devaluation for comparative purposes.

2 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 2010 Chile and New Zealand earthquakes, 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.

3 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.

4 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, net incurred losses attributable to prior years and current accident year re-estimation for the three and twelve months ended December 31, 2011 was 98.3% and 97.5%, respectively, an increase of 1.0 point and a decrease of 0.1 points versus the same periods in 2010. The claims and claim adjustment expense ratio for both periods reflects higher commercial lines casualty losses and unfavorable loss trends in LMAC's homeowners lines of business. The ratio in the year was offset by favorable surety results in LMAC and favorable homeowners results in Personal Markets. While the claims and claims adjustment expense ratio reflects unfavorable non-catastrophe results in Lloyd's Syndicate 4472 for the quarter, for the year, these results were favorable. The decrease in the underwriting expense ratio in the quarter was due to higher earned premium and lower variable compensation costs and other general expenses.

Including the impact of catastrophes, net incurred losses attributable to prior years and current accident year re-estimation, the total combined ratio for the three and twelve months ended December 31, 2011 was 104.2% and 107.4%, respectively, increases of 5.0 points and 6.2 points over the same periods in 2010. The increases in both periods reflect higher catastrophe losses, increases in asbestos and environmental reserves, and less favorable net incurred losses attributable to prior years excluding asbestos and environmental reserves. The increase in the quarter also reflects a re-estimation of current accident year losses in Commercial Markets and LMAC for commercial liability lines and unfavorable net incurred losses attributable to prior years compared to favorable loss development in 2010.

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.

Effective in the third quarter of 2010, LMAC became a SBU replacing the former Agency Markets SBU. The financial results of LMAC differ from Agency Markets' results principally due to LMAC maintaining a dedicated investment portfolio and certain expenses incurred that are specific to LMAC. As such, results of LMAC are not directly comparable to the previously reported financial information for Agency Markets.

LMAC net written premium by segment was as follows:

	Three Months Ended December 31,			**Twelve Months Ended December 31,**		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Personal	$1,394	$1,307	6.7%	$5,330	$5,203	2.4%
Commercial	1,060	1,041	1.8	4,410	4,487	(1.7)
Surety	170	164	3.7	741	731	1.4
Corporate and Other[1]	31	36	(13.9)	153	128	19.5
Total net written premium	$2,655	$2,548	4.2%	$10,634	$10,549	0.8%

1 Includes run-off operations and internal reinsurance.

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

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Commercial Lines						
Commercial multiple peril	$456	$442	3.2%	$1,865	$1,855	0.5%
Commercial automobile	240	241	(0.4)	1,042	1,072	(2.8)
Workers compensation	211	212	(0.5)	884	906	(2.4)
Surety	172	165	4.2	749	731	2.5
General liability	103	107	(3.7)	458	480	(4.6)
Other	74	67	10.4	291	284	2.5
Subtotal	$1,256	$1,234	1.8	$5,289	$5,328	(0.7)
Personal Lines						
Private passenger automobile	$872	$839	3.9	$3,195	$3,264	(2.1)
Homeowners	412	367	12.3	1,671	1,513	10.4
Other	115	108	6.5	479	444	7.9
Subtotal	$1,399	$1,314	6.5	$5,345	$5,221	2.4
Total net written premium	$2,655	$2,548	4.2%	$10,634	$10,549	0.8%

Net written premium for the three and twelve months ended December 31, 2011 was $2.655 billion and $10.634 billion, respectively, increases of $107 million and $85 million over the same periods in 2010.

Commercial lines net written premium for the three and twelve months ended December 31, 2011 was $1.256 billion and $5.289 billion, respectively, an increase of $22 million and a decrease of $39 million versus the same periods in 2010. Both periods were adversely impacted by a decline in new business premium due to a more competitive market environment and lower average policy size, partially offset by rate increases, favorable audit premiums and growth in the Surety segment largely due to increased contract premiums. The increase in the quarter was driven by favorable renewal premium as a result of rate increases and positive audits, which more than offset the decline in new business previously discussed.

Personal lines net written premium for the three and twelve months ended December 31, 2011 was $1.399 billion and $5.345 billion, respectively, increases of $85 million and $124 million over the same periods in 2010. The increases in both periods reflect higher rates, new business and retention resulting in policies in-force growth of 4.5%. The increase in the year was partially offset by the timing of private passenger automobile renewal premium due to the introduction of an annual private passenger automobile product in the second half of 2010 which resulted in formerly six month term policies that previously renewed in the first six months of the year, then an additional twelve months of premium recorded at renewal and reverting back to annual premium in 2011.

Results of Operations – Liberty Mutual Agency Corporation

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Revenues	$2,857	$2,865	(0.3%)	$11,410	$11,687	(2.4%)
PTOI before catastrophes, net incurred losses attributable to prior years, current accident year re-estimation and LP and LLC (loss) income	$260	$288	(9.7%)	$1,217	$1,311	(7.2%)
Catastrophes[1]	(45)	(114)	(60.5)	(1,385)	(586)	136.3
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	21	96	(78.1)	265	282	(6.0)
Current accident year re-estimation[3]	(34)	(12)	183.3	-	-	-
PTOI before LP and LLC (loss) income	202	258	(21.7)	97	1,007	(90.4)
LP and LLC (loss) income [4]	(2)	4	NM	-	-	-
PTOI[5]	$200	$262	(23.7%)	$97	$1,007	(90.4%)

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 and twelve months ended December 31, 2011 and zero and $10 million for the same periods in 2010.
3 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.
4 LP and LLC (loss) income is included in net investment income in the consolidated statements of income.
5 2010 PTOI excludes a certain intercompany reinsurance agreement related to run-off business which eliminates in consolidation.
NM = Not Meaningful

Pre-tax operating income for the three and twelve months ended December 31, 2011 was $200 million and $97 million, respectively, decreases of $62 million and $910 million from the same periods in 2010. The decrease in the quarter was driven by lower favorable net incurred losses attributable to prior years, primarily within the Surety segment, and unfavorable non-catastrophe loss trends in the homeowners line of business, partially offset by lower catastrophe losses (partially due to reduction of prior period catastrophe losses). The decrease in the year was driven by higher catastrophe losses, partially offset by favorable surety results. Both periods were further impacted by higher commercial lines liability losses, lower net investment income, and higher amortization of deferred acquisition costs in 2011, partially offset by lower variable compensation costs as a result of the profitability decline.

Revenues for the three and twelve months ended December 31, 2011 were $2.857 billion and $11.410 billion, respectively, decreases of $8 million and $277 million from the same periods in 2010. The major components of revenues are net premium earned, net investment income, and net realized gains.

Net premium earned for the three and twelve months ended December 31, 2011 was $2.656 billion and $10.471 billion, respectively, increases of $65 million and $155 million over the same periods in 2010. The increases in both periods reflect increased personal lines rate, retention and new business, as well as an increase in commercial lines audit premiums.

Net investment income for the three and twelve months ended December 31, 2011 was $191 million and $804 million, respectively, decreases of $21 million and $86 million from the same periods in 2010. The decreases in both periods were primarily driven by a lower invested asset base in 2011 due to intercompany dividends paid during 2010, and lower investment yields. The quarter was further impacted by lower LP and LLC investment income.

Net realized (losses) gains for the three and twelve months ended December 31, 2011 were ($16) million and $37 million, respectively, decreases of $54 million and $345 million from the same periods in 2010. Realized gains decreased during the year due to internal transfers of investments between LMAC and affiliates in 2010 that did not recur and sales of fixed income securities in 2010 related to the strategic realignment of the portfolio which did not recur in 2011. Further impacting the quarter were impairment charges taken on equity securities.

Claims, benefits and expenses for the three and twelve months ended December 31, 2011 were $2.673 billion and $11.276 billion, respectively, increases of $108 million and $855 million over the same periods in 2010. The increase in the quarter was driven by lower favorable incurred losses attributable to prior years, primarily within the Surety segment, and unfavorable non-catastrophe loss trends in the homeowners line of business, partially offset by lower catastrophe losses. The increase in the year was driven by higher catastrophe losses, partially offset by favorable surety results. Both periods were further impacted by higher commercial lines liability losses and higher amortization of deferred acquisition costs in 2011, partially offset by lower variable compensation costs.

	Three Months Ended December 31,			**Twelve Months Ended December 31,**		
LIBERTY MUTUAL AGENCY CORPORATION	**2011**	**2010**	**Change (Points)**	**2011**	**2010**	**Change (Points)**
Combined ratio before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation						
Claims and claim adjustment expense ratio	64.6%	63.5%	1.1	63.4%	63.4%	-
Underwriting expense ratio	31.3	32.1	(0.8)	31.2	31.0	0.2
Dividend ratio	0.3	0.2	0.1	0.2	0.2	-
Subtotal	96.2	95.8	0.4	94.8	94.6	0.2
Catastrophes[1]	1.7	4.4	(2.7)	13.2	5.7	7.5
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(0.8)	(3.7)	2.9	(2.5)	(2.7)	0.2
Current accident year re-estimation[2]	1.3	0.4	0.9	-	-	-
Total combined ratio[3]	98.4%	96.9%	1.5	105.5%	97.6%	7.9

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.
2 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.
3 2010 combined ratio excludes a certain intercompany reinsurance agreement related to run-off business which eliminates in consolidation.

The LMAC combined ratio before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation for the three and twelve months ended December 31, 2011 was 96.2% and 94.8%, respectively, increases of 0.4 points and 0.2 points over the same periods in 2010. The increase in the claims and claim adjustment expense ratio for the quarter reflects higher commercial lines liability losses and unfavorable loss trends in the homeowners line of business. The claims and claim adjustment expense ratio remained unchanged from the prior year primarily due to higher commercial lines liability losses, offset by favorable surety results. The decrease in the underwriting expense ratio for the quarter was primarily driven by lower variable compensation costs. The increase in the underwriting expense ratio for the year was primarily driven by higher amortization of deferred acquisition costs in 2011, partially offset by lower variable compensation costs.

Including the impact of catastrophes, net incurred losses attributable to prior years and current accident year re-estimation, the total combined ratio for the three and twelve months ended December 31, 2011 was 98.4% and 105.5%, respectively, increases of 1.5 points and 7.9 points over the same periods in 2010. The

increase in the quarter was primarily driven by less favorable net incurred losses attributable to prior years, partially offset by lower catastrophe losses. The quarter was further impacted by a current accident year re-estimation for commercial liability lines. The increase in the year was primarily driven by higher catastrophe losses and less favorable net incurred losses attributable to prior years.

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 and Ireland (as a result of the QIL acquisition in November 2011); 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 net written premium by market segment was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
International Local Businesses Total	$1,424	$1,267	12.4%	$5,233	$4,495	16.4%
- Latin America	978	845	15.7	3,542	2,955	19.9
- Europe	352	335	5.1	1,314	1,234	6.5
- Asia	94	87	8.0	377	306	23.2
Liberty International Underwriters	682	647	5.4	2,976	2,749	8.3
Total NWP	$2,106	$1,914	10.0%	$8,209	$7,244	13.3%
Foreign exchange effect on growth			(1.9%)			1.8%
NWP growth excluding foreign exchange			11.9%			11.5%

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, treaty casualty, personal accident, aviation and 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, railroad and other;
(5) LIU first party: includes marine, energy, construction, aviation and property; and
(6) LIU other: includes workers compensation, commercial automobile, surety, trade credit and crisis management.

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

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Local businesses – private passenger auto	$862	$770	11.9%	$3,132	$2,718	15.2%
Local businesses – all other[1]	562	497	13.1	2,101	1,777	18.2
Lloyd's Syndicate 4472	266	254	4.7	1,382	1,153	19.9
LIU third party	207	200	3.5	806	675	19.4
LIU inland marine program	106	109	(2.8)	405	606	(33.2)
LIU first party	85	72	18.1	314	266	18.0
LIU other	18	12	50.0	69	49	40.8
Total net written premium	$2,106	$1,914	10.0%	$8,209	$7,244	13.3%

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

Net written premium for the three and twelve months ended December 31, 2011 was $2.106 billion and $8.209 billion, respectively, increases of $192 million and $965 million over the same periods in 2010. The increases in both periods reflect organic growth in local operations, primarily Latin America, led by Venezuela (primarily due to the impact of inflation), and to a lesser extent, Asia, led by China. Europe also had organic growth, excluding Spain whose decline is a result of its continuing economic challenges. The increases also reflect the acquisition of QIL in November 2011. The increases in both periods also reflect growth in LIU, primarily driven by Lloyd's Syndicate 4472 business due to new programs that diversify our risk, such as agriculture, direct auto, trade credit, and marine; and also due to reinstatement premiums from contracts that experienced losses. LIU third party also contributed to the growth in both periods due to new business from specialty casualty lines. The increase in the year was partially offset by an increase in the amount of ceded written premium in LIU's inland marine business due to a change in a reinsurance program resulting in less net premium retained. Foreign exchange partially offset the increase in the quarter (approximately $37 million) but contributed to the increase in the year (approximately $130 million).

Results of Operations – International

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010[1]**	**Change**	**2011**	**2010[1]**	**Change**
Revenues	$2,333	$2,011	16.0%	$8,566	$7,928	8.0%
PTOI before catastrophes, net incurred losses attributable to prior years and Venezuela devaluation	$176	$182	(3.3%)	$704	$579	21.6%
Catastrophes[2]	(85)	(40)	112.5	(403)	(159)	153.5
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[3]	(68)	20	NM	(11)	92	NM
Venezuela devaluation	-	25	(100.0)	-	228	(100.0)
PTOI	$23	$187	(87.7%)	$290	$740	(60.8%)

1 Effective January 1, 2010, the Venezuela operations began applying hyper-inflationary accounting, utilizing the U.S. dollar as the functional currency.

2 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 2010 Chile and New Zealand earthquakes, 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, 2011 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.

3 Net of earned premium attributable to prior years of ($10) million and ($3) million for the three and twelve months ended December 31, 2011 and $1 million and zero for the same periods in 2010.

NM = Not Meaningful

Pre-tax operating income for the three and twelve months ended December 31, 2011 was $23 million and $290 million, respectively, decreases of $164 million and $450 million from the same periods in 2010. The decreases reflect increased catastrophe losses related to the Thailand floods (approximately $90 million) in both periods and the Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes and the tornadoes and other severe storms in the U.S. in the year. The decreases also reflect unfavorable net incurred losses attributable to prior years, compared to favorable net incurred losses attributable to prior years in 2010 (primarily within Lloyd's Syndicate 4472 business), and the impact of the Venezuela devaluation in 2010 that did not recur. Foreign exchange excluding the impact of the Venezuela devaluation in 2010 also contributed to the changes (approximately $5 million loss in the quarter and $57 million gain in the year).

Revenues for the three and twelve months ended December 31, 2011 were $2.333 billion and $8.566 billion, respectively, increases of $322 million and $638 million over the same periods in 2010. The primary components of revenues are net premium earned and net investment income.

Net premium earned for the three and twelve months ended December 31, 2011 was $2.107 billion and $7.775 billion, respectively, increases of $297 million and $619 million over the same periods in 2010. The increases in both periods reflect the previously mentioned growth in net written premium in 2011 and the last quarter of 2010, partially offset by the impact of the Venezuela devaluation in 2010.

Net investment income for the three and twelve months ended December 31, 2011 was $166 million and $637 million, respectively, increases of $17 million and $62 million over the same periods in 2010. The increases in both periods reflect a higher invested asset base due to the reinvestment of cash flow from operations, and to a lesser extent, higher yields in local operations, primarily in Latin America.

Claims, benefits and expenses for the three and twelve months ended December 31, 2011 were $2.296 billion and $8.276 billion, respectively, increases of $484 million and $1.152 billion over the same periods in 2010. The increases in both periods were the result of higher current year claims and claim adjustment expenses primarily driven by the organic growth in Latin America and Lloyd's Syndicate 4472 business, as well as higher catastrophe losses. The increases also reflect unfavorable incurred losses attributable to prior years, compared to favorable incurred losses attributable to prior years in 2010 (primarily within Lloyd's Syndicate 4472 business). The increases were partially offset by a decrease in LIU's inland marine business due to the previously mentioned reinsurance program change. Partially offsetting the increase in the year was the foreign exchange loss as a result of the Venezuela devaluation in 2010 (approximately $100 million).

INTERNATIONAL	Three Months Ended December 31,			Twelve Months Ended December 31,		
	2011	2010[1]	Change (Points)	2011	2010[1]	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	67.5%	65.3%	2.2	66.8%	68.0%	(1.2)
Underwriting expense ratio	32.1	31.8	0.3	31.6	30.8	0.8
Dividend ratio	-	-	-	-	-	-
Subtotal	99.6	97.1	2.5	98.4	98.8	(0.4)
Catastrophes[2]	4.1	2.3	1.8	5.2	2.4	2.8
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	3.2	(1.2)	4.4	0.2	(1.4)	1.6
Total combined ratio	106.9%	98.2%	8.7	103.8%	99.8%	4.0

1 2010 combined ratio has been adjusted to exclude the impact of the Venezuela devaluation for comparative purposes.

2 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 2010 Chile and New Zealand earthquakes, 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, 2011 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 and twelve months ended December 31, 2011 was 99.6% and 98.4%, respectively, an increase of 2.5 points and a decrease of 0.4 points versus the same periods in 2010. The increase in the quarter reflects unfavorable non-catastrophe claims and claim adjustment expenses, primarily within Lloyd's Syndicate 4472 business, as well as select countries in Latin America. The decrease in the year reflects favorable non-catastrophe claims and claim adjustment expenses, primarily within Lloyd's Syndicate 4472 business. The changes in both periods also reflect an increase in the underwriting expense ratio driven by LIU's inland marine business due to the previously mentioned reinsurance program change, as well as Spain due to continued economic challenges.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three and twelve months ended December 31, 2011 was 106.9% and 103.8%, respectively, increases of 8.7 points and 4.0 points over the same periods in 2010. The increases in both periods reflect the changes in the combined ratio previously discussed, as well as the impact of higher catastrophe losses and unfavorable net incurred losses attributable to prior years, compared to favorable net incurred losses attributable to prior years in 2010 (primarily within Lloyd's Syndicate 4472 business).

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 and insurance companies in the United States. Products are distributed through more than 2,000 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 net written premium by line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Private passenger automobile	$1,053	$976	7.9%	$4,511	$4,242	6.3%
Homeowners and other	624	569	9.7	2,509	2,268	10.6
Individual life	122	72	69.4	358	266	34.6
Total net written premium	$1,799	$1,617	11.3%	$7,378	$6,776	8.9%

Net written premium for the three and twelve months ended December 31, 2011 was $1.799 billion and $7.378 billion, respectively, increases of $182 million and $602 million over the same periods in 2010.

Private passenger automobile net written premium for the three and twelve months ended December 31, 2011 was $1.053 billion and $4.511 billion, respectively, increases of $77 million and $269 million over the same periods in 2010. The increases reflect 3.2% growth in policies in-force as compared to December 31, 2010 as well as rate increases.

Homeowners and other net written premium for the three and twelve months ended December 31, 2011 was $624 million and $2.509 billion, respectively, increases of $55 million and $241 million over the same periods in 2010. The increases reflect 4.2% growth in homeowners policies in-force as compared to December 31, 2010 as well as rate increases. The policy growth was achieved despite coastal management initiatives that reduced the business unit’s coastal exposure from the prior year.

Individual life net written premium for the three and twelve months ended December 31, 2011 was $122 million and $358 million, respectively, increases of $50 million and $92 million over the same periods in 2010. The increases were primarily driven by strong structured settlement sales in the second half of the year.

Results of Operations – Personal Markets

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Revenues	$2,110	$1,936	9.0%	$8,046	$7,502	7.3%
PTOI before catastrophes and net incurred losses attributable to prior years	$288	$283	1.8%	$1,206	$1,115	8.2%
Catastrophes[1]	(95)	(65)	46.2	(899)	(469)	91.7
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	3	18	(83.3)	21	27	(22.2)
PTOI	$196	$236	(16.9%)	$328	$673	(51.3%)

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.

Pre-tax operating income for the three and twelve months ended December 31, 2011 was $196 million and $328 million, respectively, decreases of $40 million and $345 million from the same periods in 2010. The decreases in both periods were largely driven by higher catastrophe losses. Both periods reflect severe storm activity in the U.S., and the year was also impacted by Hurricane Irene. In addition to higher catastrophes, both periods were impacted by adverse non-catastrophe loss experience in the auto physical damage line, partially offset by growth in net premium earned and favorable non-catastrophe results in the homeowners product line.

Revenues for the three and twelve months ended December 31, 2011 were $2.110 billion and $8.046 billion, respectively, increases of $174 million and $544 million over the same periods in 2010. The major components of revenues are net premium earned and net investment income.

Net premium earned for the three and twelve months ended December 31, 2011 was $1.877 billion and $7.114 billion, respectively, increases of $170 million and $540 million over the same periods in 2010. The increases in both periods reflect the premium earned associated with the changes in net written premium previously discussed.

Net investment income for the three and twelve months ended December 31, 2011 was $200 million and $783 million, respectively, decreases of $1 million and $9 million from the same periods in 2010. The decreases are primarily driven by lower investment yields, partially offset by a higher invested asset base due to the reinvestment of cash flow from operations.

Claims, benefits and expenses for the three and twelve months ended December 31, 2011 were $1.915 billion and $7.716 billion, respectively, increases of $213 million and $879 million over the same periods in 2010. The increases principally reflect higher catastrophe losses and an increase in losses and expenses consistent with business growth.

PERSONAL MARKETS	Three Months Ended December 31, 2011	2010	Change (Points)	Twelve Months Ended December 31, 2011	2010	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	65.1%	64.8%	0.3	63.8%	64.1%	(0.3)
Underwriting expense ratio	24.0	24.0	-	23.9	24.6	(0.7)
Dividend ratio	-	-	-	-	-	-
Subtotal	89.1	88.8	0.3	87.7	88.7	(1.0)
Catastrophes[1]	5.4	4.0	1.4	13.3	7.4	5.9
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(0.1)	(1.2)	1.1	(0.3)	(0.4)	0.1
Total combined ratio	94.4%	91.6%	2.8	100.7%	95.7%	5.0

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.

The Personal Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three and twelve months ended December 31, 2011 was 89.1% and 87.7%, respectively, an increase of 0.3 points and a decrease of 1.0 point versus the same periods in 2010. The claims and claim adjustment expense ratio declined for the year due to favorable homeowners results, partially offset by adverse loss experience within the auto physical damage line of business during the latter half of the year. In the quarter, the increased auto physical damage losses more than offset the favorable trends in the homeowners line. The underwriting expense ratio declined 0.7 points for the year primarily as a result of premium rate increases and lower variable compensation expenses. In the quarter, the impact of rate increases and variable compensation was offset by higher advertising expenditures.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three and twelve months ended December 31, 2011 was 94.4% and 100.7%, respectively, increases of 2.8 points and 5.0 points over the same periods in 2010. The increases reflect higher catastrophe losses related to several severe storms in the U.S. and lower favorable net incurred losses attributable to prior years in 2011 compared to 2010. For the year, these items are partially offset by the changes in the combined ratio previously discussed.

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 mid-sized 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 net written premium by market segment was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Commercial Markets P&C	$887	$771	15.0%	$3,986	$3,766	5.8%
Group Benefits	192	178	7.9	787	693	13.6
Summit	98	75	30.7	483	426	13.4
Liberty Mutual Reinsurance	83	72	15.3	316	295	7.1
Other Markets	-	2	(100.0)	-	3	(100.0)
Total net written premium	$1,260	$1,098	14.8%	$5,572	$5,183	7.5%

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

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Workers compensation	$605	$563	7.5%	$2,934	$2,819	4.1%
Group disability and life	192	178	7.9	787	693	13.6
General liability	187	107	74.8	650	519	25.2
Commercial automobile	111	109	1.8	442	451	(2.0)
Commercial multiple peril / fire	90	69	30.4	422	366	15.3
Other (including AVR)	75	72	4.2	337	335	0.6
Total net written premium	$1,260	$1,098	14.8%	$5,572	$5,183	7.5%

Net written premium for the three and twelve months ended December 31, 2011 was $1.260 billion and $5.572 billion, respectively, increases of $162 million and $389 million over the same periods in 2010. The increases in both periods reflect increases in workers compensation due to increases of $23 million and $183 million, respectively, in audit premium as well as higher rate and exposures. In addition, the increases in both periods reflect a large account written in the Commercial Markets P&C segment's general liability line of business and higher retention and new business writings in the group disability and life and commercial multi-peril/fire lines of business. The quarter also reflects an increase in net written premium in Liberty Mutual Reinsurance due to a change in an assumed program structure. The increase in the year also reflects a construction account with multi-year exposures in the workers compensation and general liability lines of business, a large disability account written in the first quarter, and higher new business writings in Liberty Mutual Reinsurance. The increase in the year was partially offset by the non-renewal of a large general liability account and fewer new business writings in commercial automobile. Excluding

rate and exposures, workers compensation business in-force reflects a decrease of approximately 7% in the year as a result of disciplined underwriting in a continued competitive market.

Results of Operations – Commercial Markets

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Revenues	$1,654	$1,666	(0.7%)	$6,382	$6,331	0.8%
PTOI before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation	102	69	47.8%	247	280	(11.8%)
Catastrophes[1]	(28)	7	NM	(207)	(62)	NM
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	41	20	105.0	48	60	(20.0)
Current accident year re-estimation[3]	(87)	(20)	NM	-	-	-
PTOI	$28	$76	(63.2%)	$88	$278	(68.3%)

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 2010 Chile and New Zealand earthquakes, 2011 Australia floods, 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 ($31) million and ($15) million for the three and twelve months ended December 31, 2011 and $37 million and ($75) million for the same periods in 2010. Net of amortization of deferred gains on assumed retroactive reinsurance of zero and $5 million for the three and twelve months ended December 31, 2011 and ($4) million and $34 million for the same periods in 2010. In 2011, the Company reclassified certain retroactive reinsurance results to Corporate and Other.

3 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.

NM = Not Meaningful

Pre-tax operating income for the three and twelve months ended December 31, 2011 was $28 million and $88 million, respectively, decreases of $48 million and $190 million from the same periods in 2010. The decreases in both periods reflect an increase in current accident year casualty and group disability losses, higher catastrophe losses, and lower net investment income. The quarter also includes higher losses associated with re-estimation of the current accident year in the Commercial Markets P&C segment. The decreases in both periods were partially offset by lower insurance operating costs and other expenses in addition to higher favorable development of net incurred losses attributable to prior years, net of a reclassification of certain retroactive reinsurance results to Corporate and Other in 2011.

Revenues for the three and twelve months ended December 31, 2011 were $1.654 billion and $6.382 billion, respectively, a decrease of $12 million and an increase of $51 million versus the same periods in 2010. The major components of revenues are net premium earned, net investment income and fee and other revenues.

Net premium earned for the three and twelve months ended December 31, 2011 was $1.374 billion and $5.255 billion, respectively, increases of $6 million and $111 million over the same periods in 2010. The increases in both periods reflect increases in net written premium in the group disability and life markets, a large account written in the Commercial Markets P&C segment's general liability line of business, and higher property business in-force, partially offset by lower workers compensation business in-force. The increase in the year also reflects a decrease in the estimate of prior year earned premium on loss sensitive business recorded in the twelve months ended December 31, 2010.

Net investment income for the three and twelve months ended December 31, 2011 was $218 million and $870 million, respectively, decreases of $13 million and $52 million from the same periods in 2010. The

decreases in both periods primarily reflect lower investment yields, partially offset by a higher invested asset base due to the reinvestment of cash flow from operations.

Fee and other revenues for the three and twelve months ended December 31, 2011 were $62 million and $257 million, respectively, decreases of $6 million and $10 million from the same periods in 2010. The decreases in both periods primarily reflect lower commission revenues from the Company's servicing carrier operations due to lower involuntary market premium volume in the first half of 2011. 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 and twelve months ended December 31, 2011 were $1.626 billion and $6.294 billion, respectively, increases of $35 million and $239 million over the same periods in 2010. The increases in both periods reflect an increase in current accident year casualty and group disability losses and higher catastrophe losses. The catastrophes in the quarter were attributable to the Thailand floods and unfavorable development on events that occurred prior to the fourth quarter of 2011. The increase in the quarter also includes higher losses associated with the re-estimation of the current accident year in the Commercial Markets P&C segment partially offset by favorable development of incurred losses attributable to prior accident years versus adverse development in 2010. The increase in the year reflects less favorable development of incurred losses attributable to prior accident years. The increases in both periods were partially offset by the reclassification of certain retroactive reinsurance results to Corporate and Other in 2011 and a reduction in insurance operating costs and other expenses.

	Three Months Ended December 31,			Twelve Months Ended December 31,		
COMMERCIAL MARKETS	**2011**	**2010**	**Change (Points)**	**2011**	**2010**	**Change (Points)**
Combined ratio before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation						
Claims and claim adjustment expense ratio	87.7%	87.4%	0.3	88.4%	85.7%	2.7
Underwriting expense ratio	22.3	24.4	(2.1)	24.4	24.4	-
Dividend ratio	0.4	0.3	0.1	0.5	0.6	(0.1)
Subtotal	110.4	112.1	(1.7)	113.3	110.7	2.6
Catastrophes[1]	2.3	(0.6)	2.9	4.6	1.4	3.2
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(2.9)	(2.1)	(0.8)	(0.9)	(1.2)	0.3
Current accident year re-estimation[2]	7.1	1.8	5.3	-	-	-
Total combined ratio	116.9%	111.2%	5.7	117.0%	110.9%	6.1

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 2010 Chile and New Zealand earthquakes, 2011 Australia floods, 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 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2011 and September 30, 2010.

The Commercial Markets combined ratio before catastrophes, net incurred losses attributable to prior years, and current accident year re-estimation for the three and twelve months ended December 31, 2011 was 110.4% and 113.3%, respectively, a decrease of 1.7 points and an increase of 2.6 points versus the same periods in 2010. The increases in the claims and claim adjustment expense ratio in both periods reflect an increase in current accident year casualty losses. The increase in the quarter was partially offset by several

large property losses in 2010 that did not recur. The decrease in the underwriting expense ratio in the quarter is due to lower insurance operating costs and higher 2011 current accident year earned premium driven by the large account mentioned above.

Including the impact of catastrophes, net incurred losses attributable to prior years, and current accident year re-estimation, the total combined ratio for the three and twelve months ended December 31, 2011 was 116.9% and 117.0%, respectively, increases of 5.7 points and 6.1 points over the same periods in 2010. The increases in both periods reflect the changes in the combined ratio previously discussed as well as higher catastrophe losses. The catastrophes in the quarter were attributable to the Thailand floods and unfavorable development on events that occurred prior to the fourth quarter of 2011. The quarter also includes higher losses associated with re-estimation of the current accident year in the Commercial Markets P&C segment. The increases in both periods were partially offset by higher favorable development of net incurred losses attributable to prior years, net of a reclassification of certain retroactive reinsurance results to Corporate and Other in 2011.

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 their 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.

- Certain retroactive reinsurance agreements previously reported within Commercial Markets.

Corporate and Other net written premium by line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Reinsurance, net	($146)	($152)	(3.9%)	($500)	($515)	(2.9%)
Workers compensation[1]	47	(47)	NM	(116)	(58)	100.0
Other	1	1	-	6	12	(50.0)
Total net written premium	($98)	($198)	(50.5%)	($610)	($561)	8.7%

[1] Booked as billed adjustment.
NM = Not Meaningful

Net written premium for the three and twelve months ended December 31, 2011 was ($98) million and ($610) million, respectively, an increase of $100 million and a decrease of $49 million versus the same periods in 2010. The increase in the quarter is due to a decrease in the Company's workers compensation "booked as billed" adjustment 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 program. The decrease in the year is due to an increase in the Company's workers compensation "booked as billed" adjustment and an increase in ceded premium related to the Personal Markets homeowners quota share program, partially offset by an increase in assumed premium related to the Company's internal reinsurance program.

Results of Operations – Corporate and Other

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2011**	**2010**	**Change**	**2011**	**2010**	**Change**
Revenues	$9	$72	(87.5%)	$267	($255)	NM
Pre-tax operating loss before catastrophes, net incurred losses attributable to prior years and LP and LLC income	($228)	($248)	(8.1%)	($893)	($1,051)	(15.0%)
Catastrophes[1]	19	14	35.7	213	19	NM
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	(10)	(4)	150.0	(351)	(9)	NM
- All other[3]	(75)	(4)	NM	(106)	(136)	(22.1)
Pre-tax operating loss before LP and LLC income [4]	(294)	(242)	21.5	(1,137)	(1,177)	(3.4)
LP and LLC income [5]	109	160	(31.9)	583	398	46.5
Pre-tax operating loss	($185)	($82)	125.6%	($554)	($779)	(28.9%)

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 2010 Chile and New Zealand earthquakes, 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 $4 million for the three and twelve months ended December 31, 2011 and zero and $6 million for the same periods in 2010.

2 The twelve months ended December 31, 2011 includes $294 million of strengthening of asbestos related reserves in connection with a ground-up reserve study.

3 Net of earned premium attributable to prior years of ($1) million and ($8) million for the three and twelve months ended December 31, 2011 and zero for the same periods in 2010. Net of amortization of deferred gains on retroactive reinsurance of $5 million and $129 million for the three and twelve months ended December 31, 2011 and $5 million and $20 million for the same periods in 2010. 2011 reflects a gain on commutation of two retroactive reinsurance contracts during the first quarter. 2011 includes certain retroactive reinsurance agreements previously reported within Commercial Markets.

4 Pre-tax operating loss excludes a certain intercompany reinsurance agreement related to LMAC run-off business which eliminates in consolidation.

5 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 and twelve months ended December 31, 2011 was $185 million and $554 million, respectively, an increase (in the loss) of $103 million and a decrease (in the loss) of $225 million versus the same periods in 2010. Both periods were impacted by an increase in asbestos and environmental reserves and an increase in the amount of net incurred losses attributable to prior years related to pre-2011 workers compensation business assumed from Commercial Markets, and an increase in depreciation, depletion, and impairment charges related to energy production operations, partially offset by an increase in ceded losses and expenses associated with the homeowners quota share treaty, lower corporate expenses primarily due to employee benefits, and a change in losses related to a certain reinsurance agreement. The change in the quarter is also driven by a decrease in LP and LLC income as a result of lower private equity valuations over the same period in 2010. The change in the year is also driven by a gain on the commutation of two workers compensation retroactive reinsurance agreements, internally assumed catastrophe losses related to the Chile earthquake in 2010, unfavorable prior year development related to LMAC run-off business in 2010, and an increase in LP and LLC income as a result of improved equity valuations over the same period in 2010.

Revenues for the three and twelve months ended December 31, 2011 were $9 million and $267 million, respectively, a decrease of $63 million and an increase of $522 million versus the same periods in 2010. 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 and twelve months ended December 31, 2011 was ($127) million and ($496) million, respectively, an increase of $6 million and a decrease of $5 million versus the same periods in 2010. Both periods reflect the earned premium associated with the changes in reinsurance net written premium previously discussed. Also impacting the year is a change in ceded premium related to a reinsurance agreement.

Net investment income for the three and twelve months ended December 31, 2011 was $78 million and $429 million, respectively, a decrease of $26 million and an increase of $280 million versus the same periods in 2010. The decrease in the quarter is due to a decrease in LP and LLC income as a result of declining equity valuations, versus an increase in the year due to an increase in LP and LLC equity valuations.

Net realized (losses) gains for the three and twelve months ended December 31, 2011 were ($7) million and $119 million, respectively, versus $63 million and ($34) million in the same periods in 2010. The decrease in the quarter is related to sales undertaken during 2010 in connection with the shift in the Company's tactical allocation that did not recur in 2011. The increase in the year primarily reflects gains recognized in connection with the prior sale of certain Commercial Markets policy renewal rights, gains associated with the Company's investments in the energy sector and eliminations of gains related to internal transfers of investments between LMAC and the remainder of the Company that occurred in 2010, which did not recur in 2011.

Fee and other revenues for the three and twelve months ended December 31, 2011 were $65 million and $215 million, respectively, increases of $27 million and $94 million over the same periods in 2010. The increases in both periods primarily reflect higher oil and gas revenues due to increased production.

Claims, benefits and expenses for the three and twelve months ended December 31, 2011 were $201 million and $702 million, respectively, increases of $110 million and $267 million over the same periods in 2010. The increases in both periods primarily reflect an increase in asbestos and environmental reserves, an increase in the amount of incurred losses attributable to prior years related to pre-2011 workers compensation business assumed from Commercial Markets, and an increase in depreciation, depletion, and impairment charges related to Liberty Energy, partially offset by lower corporate expenses primarily due to employee benefits. Partially offsetting the increase in the year was an increase in ceded losses and expenses associated with the homeowners quota share treaty, a gain on the commutation of two workers compensation retroactive reinsurance agreements, and internally assumed catastrophe losses related to the Chile earthquake in 2010.

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 December 31, 2011 and 2010:

$ in Millions	**As of December 31, 2011**		**As of December 31, 2010**	
Invested Assets by Type	**Carrying Value**	**% of Total**	**Carrying Value**	**% of Total**
Fixed maturities, available for sale, at fair value	$60,576	82.2%	$58,553	83.9%
Equity securities, available for sale, at fair value	1,954	2.7	1,733	2.5
LPs and LLCs	3,389	4.6	2,860	4.1
Commercial mortgage loans	1,196	1.6	1,206	1.7
Short-term investments	201	0.3	313	0.4
Other investments	400	0.5	207	0.3
Cash and cash equivalents	5,972	8.1	4,930	7.1
Total invested assets	$73,688	100.0%	$69,802	100.0%

Total invested assets as of December 31, 2011 were $73.688 billion, an increase of $3.886 billion or 5.6% over December 31, 2010. The increase reflects an increase in the valuations of LPs, increases in unrealized gains due to decreases in interest rates, the purchase of QIL, an increase in foreign exchange driven by the elimination of the Venezuela preferential exchange rate in January 2011, and the reinvestment of cash flow from operations.

Fixed maturities as of December 31, 2011 were $60.576 billion, an increase of $2.023 billion or 3.5% over December 31, 2010. The increase reflects fair value increases due to a decrease in interest rates, a valuation increase from foreign exchange as previously discussed, and the reinvestment of cash flow from operations. As of December 31, 2011, the Company had commitments to purchase various residential mortgage-backed securities at a cost of $88 million and fair value of $89 million.

Equity securities available for sale as of December 31, 2011 were $1.954 billion ($1.608 billion common stock and $346 million preferred stock) versus $1.733 billion as of December 31, 2010 ($1.230 billion

common stock and $503 million preferred stock), an increase of $221 million or 12.8% over December 31, 2010. Of the $1.608 billion of common stock at December 31, 2011, $271 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 is consistent with a shift in the Company's tactical allocation.

Investments in LPs and LLCs as of December 31, 2011 were $3.389 billion, an increase of $529 million or 18.5% over December 31, 2010. These investments consist of traditional private equity partnerships of $2.008 billion, other partnerships (primarily energy) of $827 million, and real estate partnerships of $554 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 December 31, 2011, the Company had unfunded commitments in traditional private equity partnerships, real estate, energy, and other of $900 million, $271 million, $1.052 billion, and $285 million, respectively.

Commercial mortgage loans as of December 31, 2011 were $1.196 billion (net of $18 million of loan loss reserves or 1.5% of the outstanding loan portfolio), a decrease of $10 million or 0.8% from December 31, 2010. The decrease primarily reflects $99 million in principal repayments and an increase of $4 million to the loan loss reserve, partially offset by a $93 million increase in loans. The entire commercial loan portfolio is U.S. based. As of December 31, 2011, 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 2,948 at December 31, 2010 to 3,272 at December 31, 2011. Approximately 91% of the loans are full or partial recourse to borrowers.

Cash and cash equivalents as of December 31, 2011 were $5.972 billion, an increase of $1.042 billion or 21.1% over December 31, 2010. This increase is primarily related to cash and cash equivalents acquired with the purchase of QIL in November 2011.

Regarding fair value measurements, as of December 31, 2011, excluding separate accounts and other assets, the Company reflected $3.962 billion (6.3%) 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 December 31, 2011, the Company reported $57.765 billion (91.8%) as level 2, consisting primarily of various fixed maturity securities. Finally, the Company reported $1.203 billion (1.9%) as level 3 (unobservable inputs), primarily consisting of international and privately held securities for which a market price is not readily observable.

As of December 31, 2011, no single issuer, excluding U.S. Treasuries, agency securities and mortgage-backed securities, accounted for more than 1.4% of invested assets.

The following tables summarize the Company's available for sale portfolio by security type as of December 31, 2011 and 2010:

$ 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 [1]	9,018	525	(46)	9,497
Commercial MBS	2,086	74	(3)	2,157
Other MBS and ABS [2]	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

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

$ in Millions December 31, 2010	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	$3,008	$197	($13)	$3,192
Residential MBS	9,628	455	(50)	10,033
Commercial MBS	2,378	99	(4)	2,473
Other MBS and ABS	1,661	93	(6)	1,748
U.S. state and municipal	12,414	438	(120)	12,732
Corporate and other	22,907	1,274	(206)	23,975
Foreign government securities	4,379	106	(85)	4,400
Total fixed maturities	56,375	2,662	(484)	58,553
Common stock	1,000	253	(23)	1,230
Preferred stock	552	35	(84)	503
Total equity securities	1,552	288	(107)	1,733
Total securities available for sale	$57,927	$2,950	($591)	$60,286

The following table summarizes the Company's mortgage and asset-backed fixed maturity portfolio by credit quality as of December 31, 2011:

$ in Millions	**As of December 31, 2011**							
Mortgage & Asset-Backed Fixed Maturities by Credit Quality[1]	**AAA**	**AA**	**A**	**BBB**	**BB**	**B or Lower**	**Total**	**% of Total**
SBA loans	$1,460	$-	$-	$-	$-	$-	$1,460	10.9%
GNMA residential mortgage	3,337	5	-	-	-	-	3,342	24.9
FNMA residential mortgage	2,942	-	-	-	-	-	2,942	21.9
FHLMC residential mortgage	2,643	-	-	-	-	-	2,643	19.7
Prime residential mortgage	32	38	35	14	6	226	351	2.6
Alt-A residential mortgage	1	1	28	8	9	122	169	1.3
Sub-prime residential mortgage	15	-	1	3	7	24	50	0.4
Commercial MBS	1,989	145	8	11	4	-	2,157	16.1
Non-mortgage ABS	190	26	21	54	5	19	315	2.2
Total	$12,609	$215	$93	$90	$31	$391	$13,429	100.0%
% of Total	93.9%	1.6%	0.7%	0.7%	0.2%	2.9%	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 over 98% rated AA or above with approximately 20% 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 December 31, 2011 and 2010:

$ in Millions	**As of December 31, 2011**		**As of December 31, 2010**	
Fixed Maturities by Credit Quality[1]	**Fair Value**	**% of Total**	**Fair Value**	**% of Total**
AAA	$21,732	36.0%	$22,933	39.2%
AA+, AA, AA-	10,445	17.2	10,090	17.2
A+, A, A-	11,646	19.2	10,146	17.3
BBB+, BBB, BBB-	10,289	17.0	8,917	15.2
BB+, BB, BB-	2,202	3.6	2,570	4.4
B+, B, B-	3,330	5.5	2,791	4.8
CCC or lower	932	1.5	1,106	1.9
Total fixed maturities	$60,576	100.0%	$58,553	100.0%

[1]For purposes of this disclosure, credit quality is primarily based upon average credit ratings versus the previous method which was primarily based on Standard & Poor's ratings.

The Company's allocation to investment grade securities as of December 31, 2011 remained consistent with December 31, 2010 at 89%. Overall, the average credit quality rating stands at A+ as of December 31, 2011. 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 December 31, 2011 and 2010:

$ in Millions	As of December 31, 2011		As of December 31, 2010	
Fixed Maturities by Maturity Date	**Fair Value**	**% of Total**	**Fair Value**	**% of Total**
1 year or less	$2,847	4.7%	$2,458	4.2%
Over 1 year through 5 years	17,738	29.3	16,408	28.0
Over 5 years through 10 years	14,489	23.9	13,391	22.9
Over 10 years	12,073	19.9	12,042	20.6
MBS and ABS	13,429	22.2	14,254	24.3
Total fixed maturities	$60,576	100.0%	$58,553	100.0%

During 2011, 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 and twelve months ended December 31, 2011 and 2010:

$ in Millions	Three Months Ended December 31,		Twelve Months Ended December 31,	
Net Investment Income	**2011**	**2010**	**2011**	**2010**
Taxable interest income	$632	$622	$2,487	$2,426
Tax-exempt interest income	124	118	474	539
Dividends	12	11	50	42
LP and LLC income	107	164	583	398
Commercial mortgage loans	19	19	77	73
Other investment (loss) income	(1)	4	(4)	6
Gross investment income	893	938	3,667	3,484
Investment expenses	(40)	(41)	(144)	(156)
Net investment income	$853	$897	$3,523	$3,328

Net investment income for the three and twelve months ended December 31, 2011 was $853 million and $3.523 billion, respectively, a decrease of $44 million and increase of $195 million versus the same periods in 2010. The changes in the quarter and the year primarily reflect valuation changes in LP and LLC investments. The increase in taxable interest income and the decrease in tax-exempt interest income in the year reflect a continued shift in the Company's tactical allocation.

Net Realized Gains (Losses)

The following tables summarize the Company's net realized gains (losses) for the three and twelve months ended December 31, 2011 and 2010:

$ in Millions **Net Realized Gains (Losses)**	**Sales & Dispositions**	**Impairments**	**Change in Derivatives Value**	**Total**
Three Months Ended December 31, 2011:				
Fixed maturities	$12	($7)	$-	$5
Common and preferred stock	(9)	(20)	-	(29)
Other	15	(1)	-	14
Total	$18	($28)	$-	($10)
Three Months Ended December 31, 2010:				
Fixed maturities	$97	($12)	$-	$85
Common and preferred stock	9	-	-	9
Other	15	-	1	16
Total	$121	($12)	$1	$110

$ in Millions **Net Realized Gains (Losses)**	**Sales & Dispositions**	**Impairments**	**Change in Derivatives Value**	**Total**
Twelve Months Ended December 31, 2011:				
Fixed maturities	$93	($38)	$-	$55
Common and preferred stock	68	(40)	-	28
Other	76	(1)	-	75
Total	$237	($79)	$-	$158
Twelve Months Ended December 31, 2010:				
Fixed maturities	$395	($46)	$-	$349
Common and preferred stock	50	(1)	-	49
Other	12	(9)	1	4
Total	$457	($56)	$1	$402

$ in Millions	Three Months Ended December 31,		Twelve Months Ended December 31,	
Components of Net Realized Gains (Losses)	**2011**	**2010**	**2011**	**2010**
Fixed maturities:				
Gross realized gains	$37	$103	$177	$421
Gross realized losses	(32)	(18)	(122)	(72)
Equities:				
Gross realized gains	10	9	101	52
Gross realized losses	(39)	-	(73)	(3)
Other:				
Gross realized gains	20	60	116	73
Gross realized losses	(6)	(44)	(41)	(69)
Total net realized (losses) gains	($10)	$110	$158	$402

Net realized (losses) gains for the three and twelve months ended December 31, 2011 were ($10) million and $158 million, respectively, decreases of $120 million and $244 million from the same periods in 2010. The decreases primarily reflect a net foreign exchange loss recognized in 2011 on Venezuela and Argentina securities, combined with sales undertaken during 2010 in connection with the shift in the Company's tactical allocation that did not recur in 2011. The decreases were partially offset by gains recognized in connection with the prior sale of certain Commercial Markets policy renewal rights and gains associated with the Company's investments in the energy sector.

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 December 31, 2011 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	$-	$8	$-	$-
Residential MBS	(5)	131	(41)	314
Commercial MBS	(1)	109	(2)	37
Other MBS and ABS	-	40	(2)	12
U.S. state and municipal	(1)	47	(23)	142
Corporate and other	(186)	3,865	(133)	821
Foreign government securities	(12)	289	(82)	711
Total fixed maturities	(205)	4,489	(283)	2,037
Common stock	(104)	513	(33)	124
Preferred stock	(2)	12	(101)	224
Total equities	(106)	525	(134)	348
Total	($311)	$5,014	($417)	$2,385

Unrealized losses increased from $591 million as of December 31, 2010 to $728 million as of December 31, 2011 primarily due to volatility in the equity markets. Unrealized losses less than 12 months increased from $263 million at December 31, 2010 to $311 million as of December 31, 2011. Unrealized losses 12

months or longer increased from $328 million as of December 31, 2010 to $417 million as of December 31, 2011. As of December 31, 2011, there were 805 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 and twelve months ended December 31, 2011, the Company recorded $7 million and $38 million, respectively, of fixed maturity impairment losses. The Company has concluded that the remaining gross unrealized losses of fixed maturity securities as of December 31, 2011 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 December 31, 2011 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. As of December 31, 2011, the Company has concluded that the gross unrealized losses of equity securities as of December 31, 2011 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 December 31, 2011 (including cash and cash equivalents) totaled $73.688 billion.

Short-term debt and current maturities of long-term debt outstanding as of December 31, 2011 and December 31, 2010 were as follows:

$ in Millions	**As of December 31, 2011**	**As of December 31, 2010**
Commercial paper	$-	$-
Current maturities of long-term debt[1]	205	1
Total short-term debt and current maturities of long-term debt	$205	$1

[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 December 31, 2011 and December 31, 2010 was as follows:

$ in Millions	As of December 31, 2011	As of December 31, 2010
7.25% Notes, due 2012	$ -	$204
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	49
6.70% Notes, due 2016	249	249
7.00% Junior Subordinated notes, due 2067[1]	300	300
5.00% Notes, due 2021	600	-
8.50% Surplus notes, due 2025	140	140
7.875% Surplus notes, due 2026	227	227
7.625% Notes, due 2028	3	3
7.00% Notes, due 2034	231	231
6.50% Notes, due 2035	471	471
7.50% Notes, due 2036	19	440
7.80% Junior Subordinated notes, due 2087[2]	700	700
10.75% Junior Subordinated notes, due 2088[3]	981	1,250
7.697% Surplus notes, due 2097	435	435
Subtotal	5,389	5,684
Unamortized discount	(48)	(49)
Total long-term	$5,341	$5,635

[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 and twelve month periods ended December 31, 2011, the Company repurchased $135 million and $269 million, respectively, of the 10.75% Junior Subordinated notes due 2088. Pre-tax losses of $33 million and $70 million, 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. LMFIC is a member of the Federal Home Loan Bank of Chicago as of 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 June 10, 2011, PIC borrowed $12 million under its agreement. On December 9, 2011, the borrowing was repaid at maturity. As of December 31, 2011, no borrowings were outstanding.

On October 24, 2011, LMAC and Ohio Casualty Corporation ("OCC") 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 December 31, 2011, there was no 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 on the transactions which is included in loss on extinguishment of debt in the accompanying consolidated statements of income. After completion of the tender offer and subsequent open market purchase, $19 million aggregate principal amount of the 2036 Notes remains outstanding.

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 December 31, 2011, 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 maintains a £10 million overdraft facility which expires on March 31, 2012. The facility is available to provide working capital to the Company's international operations. As of December 31, 2011, no borrowings were outstanding under the facility.

Interest Expense

Consolidated interest expense for the three and twelve months ended December 31, 2011 was $106 million and $439 million, decreases of $5 million and $17 million from the same periods in 2010. The decreases reflect 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 and 2021 Notes is $30 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 December 31, 2011, the Company, through its downstream subsidiary LMGI, had $4.823 billion of debt outstanding, excluding discount. This

amount includes a short-term loan of $121 million from LMIC that was paid off in full on January 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**	**2011**
LMIC	469%	503%	$1,359	$65
LMFIC	458%	551%	-	$65
EICOW	623%	671%	$49	$50

[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 twelve months ended December 31, 2011. Available dividend capacity as of December 31, 2011 is calculated as 2012 dividend capacity less dividends paid for the preceding 12 months.

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 adviser 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 and twelve months ended December 31, 2011, LCS recorded $89 million and $353 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 $15.701 billion and $16.039 billion at December 31, 2011 and December 31, 2010, respectively. The decrease in surplus primarily reflects a net loss of $471 million (the sum of earnings from the Company's 58 domestic insurance companies and dividends from subsidiaries), other changes in surplus of ($341) million, primarily related to dividends to stockholders, amortization expense, and an increase in non-admitted assets, and unaffiliated unrealized losses of $110 million, partially offset by affiliated unrealized gains of $584 million.

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 2010 amounts to conform with the 2011 presentation.

Adoption of New Accounting Standards

There were no accounting standards adopted through the fourth quarter of 2011 that had a material financial statement impact on the Company.

Future Adoption of New Accounting Standards

In October 2010, the FASB issued 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 deferred 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 is required to adopt ASU 2010-26 effective January 1, 2012. The Company is applying the guidance retrospectively, and the cumulative effect of the change in the method of accounting will result in a decrease in the opening balance of policyholders'equity as of January 1, 2012 of $265 million, net of tax.

None of the other accounting standards issued for the fourth quarter of 2011 will have a material financial statement impact on the Company. See Note 1 in the Audited Consolidated Financial Statements as of and for the year ended December 31, 2011 for further discussion of the Company's significant accounting policies.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were $50.228 billion and $48.059 billion as of December 31, 2011 and December 31, 2010, respectively. The increase resulted primarily from large catastrophe losses in 2011.

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 increased $143 million from $1.189 billion as of December 31, 2010 to $1.332 billion as of December 31, 2011.

In the third quarter of 2011, the Company completed a ground-up asbestos study 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 $13.272 billion and $14.310 billion at December 31, 2011 and 2010, respectively, net of allowance for doubtful accounts of $326 million and $393 million, respectively. The decrease in reinsurance recoverables is primarily due to the commutations of two excess of loss retroactive reinsurance agreements. Included in these balances are $941 million and $965 million of paid recoverables and $12.657 billion and $13.738 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 ("the 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 December 31, 2011. Collateral held against outstanding gross reinsurance recoverable balances was $4.699 billion and $5.359 billion at December 31, 2011 and 2010, 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 December 31, 2011.

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 December 31, 2011 and 2010, deferred gains related to these reinsurance arrangements were $315 million and $550 million respectively, and are included in other liabilities within the consolidated balance sheets. Interest credited to the funds held balances for the years ended December 31, 2011, 2010, and 2009 was $105 million, $118 million, and $117 million, respectively. Deferred gain amortization was $129 million, $54 million, and $72 million for the years ended December 31, 2011, 2010, and 2009, respectively. Reinsurance recoverables related to these transactions including experience related profit accruals were $1.217 billion and $1.947 billion as of December 31, 2011 and 2010, 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. Approximately $17 million and $10 million of additional losses were ceded to these retroactive and prospective contracts, respectively, during the year ended December 31, 2011, with additional premium of $11 million and $7 million, respectively. Additional premium and loss activity on these retroactive and prospective contracts was immaterial in 2010 and 2009. The income statement impact of ceding the additional losses and premium on the 2001 covered accident year period was deferred for GAAP purposes and is amortized into income using the effective interest method over the estimated settlement period. The retroactive portion of the aggregate stop loss program is included in the preceding paragraph.

In 2007, the Company entered into a multi-year property catastrophe reinsurance agreement with Mystic Re II Ltd. ("Mystic Re II"), a Cayman Islands domiciled reinsurer, to provide $150 million of reinsurance coverage for the Company and its affiliates in the event of a Northeast and/or Florida hurricane event. In the first quarter 2009, the Company entered into another agreement with Mystic Re II to provide $225 million of additional reinsurance coverage for the Company in the event of a U.S. hurricane or earthquake event. The reinsurance agreements are collateralized through a trust and guarantee received by Mystic Re II from the issuance of catastrophe bonds and 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 Company has not recorded any recoveries under these programs. Mystic Re II does not have any other reinsurance in force. The 2007 reinsurance agreement terminated on June 7, 2011. Since no recoveries were recorded under this program, the associated collateral was released.

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 flows 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 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 December 31, 2011, 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 December 31, 2011, 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 $250 million and $94 million as of December 31, 2011 and December 31, 2010, respectively and the Company's maximum exposure to loss was $309 million and $123 million as of December 31, 2011 and December 31, 2010, 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. As of December 31, 2011, the Company had no material derivative agreements in place.

Deferred Acquisition Costs

Total deferred policy acquisition costs were $2.808 billion and $2.771 billion as of December 31, 2011 and December 31, 2010, respectively. Deferred policy acquisition costs are costs that vary with, and are primarily related to, the acquisition of new and renewal insurance and investment contracts that are deferred and amortized over the respective policy terms. Deferred acquisition costs are reviewed annually for recoverability. Investment income is considered in the recoverability assessment. For short-duration insurance contracts, acquisition costs include commissions, underwriting expenses, and premium taxes and assessments. For long-duration insurance contracts, these costs include first year commissions in excess of annual renewal commissions and variable sales and underwriting expenses.

Goodwill

Goodwill assets were $4.766 billion and $4.750 billion as of December 31, 2011 and December 31, 2010, 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. In 2011, the Company utilized the qualitative and quantitative approaches across its business units. In 2010, the Company utilized only the quantitative approach.

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.

Deferred Income Taxes

The net deferred income tax asset was $815 million and $796 million as of December 31, 2011 and December 31, 2010, respectively, net of a valuation allowance of $136 million and $153 million, respectively. The net increase in the Company's net deferred income tax asset is primarily due to the future anticipated tax benefit of net operating losses carried forward and the change in net unrealized capital gains and losses on certain investments. The overall decrease in the valuation allowance is primarily due to 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. Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax bases of assets and liabilities at the enacted tax rates. The principal assets and liabilities giving rise to such differences are 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, 2010	$321
Additions based on tax positions related to current year	7
Additions for tax positions of prior years	55
Reductions for tax positions of prior years	(12)
Settlements	(39)
Balance at December 31, 2011	$332

Included in the tabular roll forward of unrecognized tax benefits is interest in the amount of $78 million and $84 million as of December 31, 2011 and December 31, 2010, respectively.

Included in the balance at December 31, 2011, is $148 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 December 31, 2011 and 2010, the Company recognized ($2) million and ($7) million in interest and penalties, respectively. During the years ended

December 31, 2011 and 2010, the Company recognized approximately $2 million and ($2) million in interest and penalties, respectively. The Company had approximately $82 million and $80 million of interest and penalties accrued at December 31, 2011 and December 31, 2010, 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.

Other

On April 28, 2011, affiliates of the Company and Anglo Irish Bank Corporation Limited ("Anglo") entered into a joint venture to create an Irish insurance company, Liberty Mutual Direct Insurance Company Limited ("LMDI"), and for the purchase of assets and assumption of liabilities of QIL (Under Administration) related to QIL's marketing and underwriting of insurance policies in the Republic of Ireland. Following the receipt of the requisite approvals and LMDI's insurance license, the transaction closed on November 11, 2011. Upon the closing of the transaction, an affiliate of the Company, Liberty ITB UK and Europe Limited, contributed €103 million to capitalize the joint venture and an affiliate of Anglo contributed €99 million. Through such contributions, the Company obtained indirect ownership of 51% of the joint venture, which wholly owns LMDI. LMDI also provides services related to QIL's business in the United Kingdom.

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 2010 net 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.