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

Year Ended December 31, 2012

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

The following discussion highlights significant factors influencing results of operations and changes in financial position of Liberty Mutual Holding Company Inc., the parent corporation of the Liberty Mutual Insurance group of entities (the "Company" or "LMHC"), for the three and twelve months ended December 31, 2012 and 2011. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's December 31, 2012 Unaudited Consolidated Financial Statements, and Fourth Quarter 2012 Financial Supplement located on the Company's Investor Relations website at www.libertymutual.com/investors. The Company's discussions related to net income are presented in conformity with U.S. generally accepted accounting principles ("GAAP") on an after-tax basis. All other discussions are presented on a pre-tax GAAP basis, unless otherwise noted. Further, the Company notes that it may make material information regarding the Company available to the public, from time to time, via the Company's Investor Relations website at www.libertymutual.com/investors (or any successor site).

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Cautionary Statement Regarding Forward Looking Statements

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

Some of the factors that could cause actual results to differ include, but are not limited to the following: the occurrence of catastrophic events (including terrorist acts, hurricanes, hail, tornadoes, tsunamis, earthquakes, floods, snowfall and winter conditions); inadequacy of loss reserves; adverse developments involving asbestos, environmental or toxic tort claims and litigation; adverse developments in the cost, availability or ability to collect reinsurance; disruptions to the Company's relationships with its independent agents and brokers; financial disruption or a prolonged economic downturn; the performance of the Company's investment portfolios; a rise in interest rates; risks inherent in the Company's alternative investments in private limited partnerships ("LP") and limited liability companies ("LLC"); difficulty in valuing certain of the Company's investments; subjectivity in the determination of the amount of impairments taken on the Company's investments; unfavorable outcomes from litigation and other legal proceedings, including the effects of emerging claim and coverage issues and investigations by state and federal authorities; the Company's exposure to credit risk in certain of its business operations; terrorist acts; the Company's inability to obtain price increases or maintain market share due to competition or otherwise; inadequacy of the Company's pricing models; changes to insurance laws and regulations; changes in the amount of statutory capital that the Company must hold to maintain its financial strength and credit ratings; regulatory restrictions on the Company's ability to change its methods of marketing and underwriting in certain areas; assessments for guaranty funds and mandatory pooling arrangements; a downgrade in the Company's claims-paying and financial strength ratings; the ability of the Company's subsidiaries to pay dividends to the Company; inflation, including inflation in medical costs and automobile and home repair costs; the cyclicality of the property and casualty insurance industry; political, legal, operational and other risks faced by the Company's international business; potentially high severity losses involving the Company's surety products; loss or significant restriction on the Company's ability to use credit scoring in the pricing and underwriting of personal lines policies; inadequacy of the Company's controls to ensure compliance with legal and regulatory standards; changes in federal or state tax laws; risks arising out of the Company's securities lending program; the Company's utilization of information technology systems and its implementation of technology innovations; difficulties with technology or data security; insufficiency of the Company's business continuity plan in the event of a disaster; the Company's ability to successfully integrate operations, personnel and technology from its acquisitions; insufficiency of the Company's enterprise risk management models and modeling techniques; and changing climate conditions. The Company's forward looking statements speak only as of the date of this report or as of the date they are made and should be regarded solely as the Company's current plans, estimates and beliefs. For a detailed discussion of these and other cautionary statements, visit the Company's Investor Relations website at www.libertymutual.com/investors. The Company undertakes no obligation to update these forward looking statements.

EXECUTIVE SUMMARY

The following highlights do not address all of the matters covered in the other sections of Management's Discussion & Analysis of Financial Condition and Results of Operations or contain all of the information that may be important to the investing public. This summary should be read in conjunction with the other sections of Management's Discussion & Analysis of Financial Condition and Results of Operations and the Company's 2012 Unaudited Consolidated Financial Statements.

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

- Revenues for the three months ended December 31, 2012 were $9.628 billion, an increase of $665 million or 7.4% over the same period in 2011.
- Net written premium ("NWP") for the three months ended December 31, 2012 was $8.491 billion, an increase of $783 million or 10.2% over the same period in 2011.
- Pre-tax operating loss before LP and LLC income for the three months ended December 31, 2012 was $622 million, which includes approximately $886 million of catastrophe losses due to Superstorm Sandy, versus pre-tax operating income ("PTOI") before LP and LLC income of $156 million in the same period in 2011.
- Pre-tax operating loss for the three months ended December 31, 2012 was $523 million versus PTOI of $263 million in the same period in 2011.
- Strategic Business Unit ("SBU") realignment expenses for the three months ended December 31, 2012 were $57 million versus zero for the same period in 2011.
- Loss on extinguishment of debt for the three months ended December 31, 2012 was $30 million, a decrease of $3 million or 9.1% from the same period in 2011. $56 million of debt with a weighted average interest rate of 10.75% was repurchased in the quarter. There was no debt issued and there were no debt maturities in the quarter.
- Net loss attributable to LMHC for the three months ended December 31, 2012 was $234 million versus $285 million net income attributable to LMHC in the same period in 2011.
- Cash flow from operations for the three months ended December 31, 2012 was $667 million, an increase of $31 million or 4.9% over the same period in 2011.
- 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, 2012 was 97.6%, a decrease of 0.8 points from the same period in 2011. 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, 2012 increased 8.7 points to 112.9%.

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[1]Catastrophes include all current and prior accident year catastrophe losses excluding losses related to the Company's external reinsurance assumed lines except for Hurricane Isaac, the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods, the 2011 and 2012 tornadoes and other severe storms in the U.S. including Superstorm Sandy. 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, 2012 and September 30, 2011.

Twelve Months Ended December 31, 2012 - Consolidated Results of Operations

- Revenues for the twelve months ended December 31, 2012 were $36.944 billion, an increase of $2.273 billion or 6.6% over the same period in 2011.
- NWP for the twelve months ended December 31, 2012 was $33.555 billion, an increase of $2.360 billion or 7.6% over the same period in 2011.
- PTOI before LP and LLC income for the twelve months ended December 31, 2012 was $351 million versus $345 million of pre-tax operating loss before LP and LLC income in the same period in 2011.
- PTOI for the twelve months ended December 31, 2012 was $704 million, an increase of $466 million or 195.8% over the same period in 2011.
- SBU realignment expenses for the twelve months ended December 31, 2012 were $99 million versus zero for the same period in 2011.
- Loss on extinguishment of debt for the twelve months ended December 31, 2012 was $193 million, an increase of $83 million or 75.5% over the same period in 2011. $893 million of debt with a weighted average interest rate of 8.32% was repurchased in 2012, $1.800 billion was issued with a weighted average interest rate of 5.45%, and $204 million of debt matured.
- Net income attributable to LMHC for the twelve months ended December 31, 2012 was $829 million, an increase of $471 million or 131.6% over the same period in 2011.
- Cash flow from operations for the twelve months ended December 31, 2012 was $2.911 billion, an increase of $753 million or 34.9% over the same period in 2011.
- The consolidated combined ratio before catastrophes and net incurred losses attributable to prior years for the twelve months ended December 31, 2012 was 97.1%, a decrease of 0.5 points from the same period in 2011. Including the impact of catastrophes and net incurred losses attributable to prior years, the Company's combined ratio for the twelve months ended December 31, 2012 decreased 2.8 points to 104.7%.

Financial Condition as of December 31, 2012

- Total assets were $120.060 billion as of December 31, 2012, an increase of $3.209 billion over December 31, 2011.
- Total equity was $18.525 billion as of December 31, 2012, an increase of $926 million over December 31, 2011.

Subsequent Events

Effective February 13, 2013, the Venezuelan government devalued its currency, announcing that the fixed official exchange rate would be changed to 6.3 BsF to 1 U.S. dollar rate. While it is expected that the devaluation will reduce various financial statement amounts, including net written premium and claims and claim adjustment expense reserves in 2013, the anticipated impact to consolidated policyholders' equity is not expected to be material. Had the devaluation occurred effective January 1, 2012, net written premium and claims and claim adjustment expense reserves would have been reduced by $581 million and $181million, respectively.

CONSOLIDATED RESULTS OF OPERATIONS

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

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

On July 24, 2012, the Company announced the realignment of its four SBUs. The four new SBUs are as follows:

- Personal Insurance includes all domestic personal lines business. Liberty Mutual Insurance and Safeco Insurance brands and products are being maintained, and distribution channels continue to be managed separately. Personal Insurance also includes the Individual Life business, which sells life and annuity products.

- Commercial Insurance serves traditional domestic commercial property and casualty accounts of all sizes and includes Summit and Group Benefits. As part of the realignment, the brands for the regional companies will no longer be used and are being replaced by a regional operating model under the Liberty Mutual Insurance brand.

- Liberty International comprises local country operations.

- Global Specialty includes Liberty International Underwriters ("LIU") including Liberty's Lloyd's Syndicate 4472 ("Syndicate 4472"), Liberty Mutual Surety ("LMS"), and Liberty Mutual Reinsurance ("LMR").

All historical results have been restated to reflect this change.

Overview – Consolidated

Consolidated NWP by significant line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Private passenger automobile	$3,059	$2,788	9.7%	$11,662	$10,848	7.5%
Homeowners	1,182	862	37.1	4,100	3,456	18.6
Workers compensation - Voluntary	828	817	1.3	3,598	3,579	0.5
Workers compensation - Involuntary	34	19	78.9	136	82	65.9
Commercial multiple-peril / fire	597	604	(1.2)	2,566	2,523	1.7
Commercial automobile	474	430	10.2	1,886	1,789	5.4
Syndicate 4472	281	267	5.2	1,580	1,451	8.9
General liability	301	325	(7.4)	1,281	1,286	(0.4)
Group disability and life	300	278	7.9	1,160	1,104	5.1
LIU third party	246	224	9.8	954	852	12.0
Individual life and health	263	235	11.9	903	771	17.1
Surety	172	171	0.6	721	749	(3.7)
LIU inland marine program	146	106	37.7	522	405	28.9
LIU first party	102	93	9.7	384	369	4.1
Other[1] (including AVR)	506	489	3.5	2,102	1,931	8.9
Total NWP[2]	$8,491	$7,708	10.2%	$33,555	$31,195	7.6%

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

Consolidated NWP by SBU was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Personal Insurance	$3,518	$3,193	10.2%	$13,910	$12,708	9.5%
Commercial Insurance	2,225	2,266	(1.8)	9,736	9,819	(0.8)
Liberty International	1,625	1,424	14.1	5,747	5,233	9.8
Global Specialty	972	935	4.0	4,310	4,033	6.9
Corporate and Other	151	(110)	NM	(148)	(598)	(75.3)
Total NWP	$8,491	$7,708	10.2%	$33,555	$31,195	7.6%
Foreign exchange effect on growth			(0.5%)			(1.1%)
NWP growth excluding foreign exchange			10.7%			8.7%

Major drivers of NWP growth were as follows:

$ in Millions	Three Months Ended December 31, 2012	2011	$ Change	Points Attribution	Twelve Months Ended December 31, 2012	2011	$ Change	Points Attribution
Total NWP	$8,491	$7,708	$783	10.2	$33,555	$31,195	$2,360	7.6
Components of Growth:								
International local businesses (ex foreign exchange)	1,665	1,424	241	3.1	6,044	5,233	811	2.6
Domestic personal automobile	2,094	1,926	168	2.2	8,306	7,716	590	1.9
-Domestic homeowners	1,104	976	128	1.7	4,438	3,938	500	1.6
-Homeowners quota share	11	(173)	184	2.4	(577)	(697)	120	0.4
Total domestic homeowners	1,115	803	312	4.1	3,861	3,241	620	2.0
LIU (ex foreign exchange)	508	441	67	0.9	1,958	1,695	263	0.8
Syndicate 4472 (ex foreign exchange)	280	267	13	0.2	1,596	1,451	145	0.5
Domestic individual life	128	124	4	0.1	417	365	52	0.2
Domestic group disability and life	197	192	5	0.1	788	787	1	-
Surety	172	171	1	-	721	749	(28)	(0.1)
Other commercial lines	2,369	2,360	9	-	10,195	9,958	237	0.8
Foreign exchange	(37)	-	(37)	(0.5)	(331)	-	(331)	(1.1)
Total NWP	$8,491	$7,708	$783	10.2	$33,555	$31,195	$2,360	7.6

Consolidated NWP by geographic distribution channels was as follows:

$ in Millions	Three Months Ended December 31, 2012	2011	Change	Twelve Months Ended December 31, 2012	2011	Change
U.S.	$6,389	$5,822	9.7%	$25,619	$23,899	7.2%
International[1]	2,102	1,886	11.5	7,936	7,296	8.8
Total NWP	$8,491	$7,708	10.2%	$33,555	$31,195	7.6%

1 Excludes domestically written business in Global Specialty's LIU market segment.

NWP for the three and twelve months ended December 31, 2012 was $8.491 billion and $33.555 billion, respectively, increases of $783 million and $2.360 billion over the same periods in 2011. Significant changes by major line of business include:

- Private passenger automobile NWP increased $271 million and $814 million in the quarter and year, respectively. The increases in both periods primarily reflect growth of policies in-force and rate increases in Personal Insurance, organic growth in Liberty International, primarily in Latin America (Venezuela), and the acquisition of Quinn Insurance Limited ("QIL") in Ireland in November 2011.
- Homeowners NWP increased $320 million and $644 million in the quarter and year, respectively. The increases in both periods primarily reflect growth of policies in-force and rate increases in Personal Insurance.
- Workers compensation NWP increased $26 million and $73 million in the quarter and year, respectively. The increases in both periods primarily reflect rate increases, audit premiums and the "booked as billed" adjustment in Corporate and Other, substantially offset by exposure reductions of 12%.

- Commercial automobile NWP increased $44 million and $97 million in the quarter and year, respectively. The increases in both periods primarily reflect recent acquisitions in Liberty International.
- Syndicate 4472 NWP increased $14 million and $129 million in the quarter and year, respectively. The increases in both periods were largely due to rate increases and new business.
- LIU third party NWP increased $22 million and $102 million in the quarter and year, respectively. The increases in both periods primarily reflect favorable rates and new business.
- Individual life and health NWP increased $28 million and $132 million in the quarter and year, respectively. The increase in the year was primarily driven by organic growth including higher renewal premium in Venezuela and an increase in structured settlement sales in Personal Insurance.
- LIU inland marine program NWP increased $40 million and $117 million in the quarter and year, respectively. The increases in both periods primarily reflect subscriber growth, pricing mix and the inception of a program in Japan in 2012.

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

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

Results of Operations – Consolidated

$ in Millions	Three Months Ended December 31,			Twelve Months Ended December 31,		
	2012	2011	Change	2012	2011	Change
Revenues	$9,628	$8,963	7.4%	$36,944	$34,671	6.6%
PTOI before catastrophes, net incurred losses attributable to prior years, current accident year re-estimation and LP and LLC income	$559	$594	(5.9%)	$2,581	$2,458	5.0%
Catastrophes[1]	(843)	(234)	NM	(1,860)	(2,681)	(30.6)
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	2	(10)	NM	(56)	(351)	(84.0)
- All other[3]	(319)	(74)	NM	(314)	229	NM
Current accident year re-estimation[4]	(21)	(120)	(82.5)	-	-	-
Pre-tax operating (loss) income before LP and LLC income	(622)	156	NM	351	(345)	NM
LP and LLC income[5]	99	107	(7.5)	353	583	(39.5)
Pre-tax operating (loss) income	(523)	263	NM	704	238	195.8
Net realized gains (losses)	185	(10)	NM	534	158	NM
SBU realignment expenses	(57)	-	NM	(99)	-	NM
Loss on extinguishment of debt	(30)	(33)	(9.1)	(193)	(110)	75.5
Pre-tax (loss) income	(425)	220	NM	946	286	NM
Income tax benefit (expense)	225	63	NM	(90)	75	NM
Consolidated net (loss) income	(200)	283	NM	856	361	137.1
Less: Net income (loss) attributable to non-controlling interest	34	(2)	NM	27	3	NM
Net (loss) income attributable to LMHC	($234)	$285	NM	$829	$358	131.6%
Cash flow from operations	$667	$636	4.9%	$2,911	$2,158	34.9%

1 Catastrophes include all current and prior accident year catastrophe losses excluding losses related to the Company's external reinsurance assumed lines except for Hurricane Isaac, the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods, the 2011 and 2012 tornadoes and other severe storms in the U.S. including Superstorm Sandy. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 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 $3 million and $56 million for the three and twelve months ended December 31, 2012 and ($41) million and ($26) million for the same periods in 2011. Net of amortization of deferred (losses) gains on retroactive reinsurance of ($3) million and $29 million for the three and twelve months ended December 31, 2012 and $5 million and $134 million for the same periods in 2011. 2011 reflects 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, 2012 and September 30, 2011.

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

NM = Not Meaningful

Pre-tax operating (loss) income for the three and twelve months ended December 31, 2012 was ($523) million and $704 million, respectively, versus $263 million and $238 million in the same periods in 2011. Both periods were favorably impacted by current accident year underwriting improvement in workers compensation, commercial multiple-peril and commercial auto, favorable loss trends in personal auto and homeowners lines of business, growth in personal auto and homeowners, and exposure reductions in workers compensation partially offset by increased surety losses, unfavorable net incurred losses attributable to prior years (primarily pre-2011 workers compensation business and LIU third party) and lower LP and LLC income. Full year results also improved due to lower catastrophe losses. The quarter included a loss of $886 million from Superstorm Sandy.

Revenues for the three and twelve months ended December 31, 2012 were $9.628 billion and $36.944 billion, respectively, increases of $665 million and $2.273 billion over the same periods in 2011. The major components of revenues are net premium earned, net investment income, net realized gains, and fee and other revenues.

Net premium earned for the three and twelve months ended December 31, 2012 was $8.389 billion and $32.165 billion, respectively, increases of $502 million and $2.046 billion over the same periods in 2011. The increases in both periods primarily reflect strong written premium growth in the prior twelve months, including rate increases, audit premiums and the acquisition of QIL, partially offset by the impact of foreign exchange.

Net investment income for the three and twelve months ended December 31, 2012 was $788 million and $3.237 billion, respectively, decreases of $65 million and $286 million from the same periods in 2011. The decrease in the year and to a lesser extent in the quarter reflects lower LP and LLC investment income. In addition, both periods reflect a decrease in interest income due to lower investment yields attributable to a tactical portfolio realignment along with the low yield environment overall.

Net realized gains for the three and twelve months ended December 31, 2012 were $185 million and $534 million, respectively, increases of $195 million and $376 million over the same periods in 2011. The increases in the quarter and year primarily relate to gains recognized from security sales as part of a tactical portfolio realignment and gains on the sale of investments in the energy sector. Additionally, the year was impacted by a gain recognized from the sale of a business segment in Argentina and contingent consideration recognized in connection with the prior sale of certain Commercial Insurance policy renewal rights in 2009, partially offset by increased impairments due to market volatility.

Fee and other revenues for the three and twelve months ended December 31, 2012 were $266 million and $1.008 billion, respectively, increases of $33 million and $137 million over the same periods in 2011. The increases in both periods primarily reflect higher oil and gas revenues in Corporate and Other due to increased production, increases in Commercial Insurance revenues from servicing carrier operations due to higher involuntary market premium volume, and third-party administrator fee income and higher premium finance revenues in Liberty International.

Claims, benefits and expenses for the three and twelve months ended December 31, 2012 were $9.966 billion and $35.706 billion, respectively, increases of $1.256 billion and $1.431 billion over the same periods in 2011. The increases in both periods reflect increases in losses and expenses consistent with business growth. Both periods were favorably impacted by decreased current accident year losses in the workers compensation, commercial multiple-peril, commercial and personal auto and homeowners lines of business partially offset by increased surety losses and unfavorable incurred losses attributable to prior years, primarily pre-2011 workers compensation business and LIU third party. The quarter was also impacted by a $609 million increase in catastrophe losses due to Superstorm Sandy, which generated a loss of $886 million. The year was also favorably impacted by reduced catastrophes and asbestos and environmental reserves partially offset by variable compensation costs and unfavorable incurred losses attributable to prior years.

Expenses related to the Company's realignment of its SBUs for the three and twelve months ended December 31, 2012 were $57 million and $99 million, respectively. The expense for the year includes a $33 million impairment of an intangible asset related to the decision to discontinue the regional company brands.

Loss on extinguishment of debt for the three and twelve months ended December 31, 2012 was $30 million and $193 million, respectively, a decrease of $3 million and an increase of $83 million versus the same periods in 2011, primarily resulting from two tender offers completed in the second quarter of 2012. For the twelve months ended December 31, 2012, $893 million of debt with a weighted average interest rate of 8.32% was repurchased and $1.800 billion was issued with a weighted average interest rate of 5.45%.

Income tax benefit (expense) for the three and twelve months ended December 31, 2012 was $225 million and ($90) million, respectively, versus $63 million and $75 million for the same periods in 2011. The Company's effective tax rate for the three and twelve months ended December 31, 2012 was 53% and 10% compared to (29%) and (26%) for the same periods in 2011. For the three months ended December 31, 2012 the Company reported an income tax benefit on a pre-tax loss, compared to reporting an income tax benefit on pre-tax income for the three months ended December 31, 2011. For the twelve months ended December 31, 2012 the Company reported a tax provision on pre-tax income as compared to reporting a tax benefit on lower pre-tax income for the same period in 2011. The effective tax rate for the twelve months ended December 31, 2012 increased over the effective tax rate for the same period in 2011 primarily due to increases in pre-tax income and the change in valuation allowance related to foreign subsidiaries, offset by increased general business credits, net benefit of foreign taxes and revisions to prior-year estimates. The Company's effective tax rate differs from the federal statutory rate of 35% principally due to tax-exempt investment income, foreign taxes, general business credits, revisions to prior-year estimates, and the change in valuation allowance.

Net (loss) income attributable to LMHC for the three and twelve months ended December 31, 2012 was ($234) million and $829 million, respectively, versus $285 million and $358 million in the same periods in 2011.

Cash flow from operations for the three and twelve months ended December 31, 2012 was $667 million and $2.911 billion, increases of $31 million and $753 million over the same periods in 2011. The increases in both periods reflect higher premium collections partially offset by the impact of QIL cash outflow due to loss reserve liquidation and non-catastrophe paid losses and expenses consistent with business growth. The quarter reflects higher catastrophe loss payments primarily due to Superstorm Sandy. The current year was also impacted by a federal income tax refund and lower catastrophe loss payments, partially offset by additional pension funding.

	Three Months Ended December 31,			Twelve Months Ended December 31,		
	2012	**2011**	**Change (Points)**	**2012**	**2011**	**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	68.5%	70.1%	(1.6)	67.8%	69.0%	(1.2)
Underwriting expense ratio	29.0	28.1	0.9	29.2	28.4	0.8
Dividend ratio	0.1	0.2	(0.1)	0.1	0.2	(0.1)
Subtotal	97.6	98.4	(0.8)	97.1	97.6	(0.5)
Catastrophes[1]	10.5	3.0	7.5	6.0	9.3	(3.3)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	0.7	0.1	0.6	0.5	1.3	(0.8)
- All other	3.8	1.1	2.7	1.1	(0.7)	1.8
Current accident year re-estimation[2]	0.3	1.6	(1.3)	-	-	-
Total combined ratio[3]	112.9%	104.2%	8.7	104.7%	107.5%	(2.8)

1 Catastrophes include all current and prior accident year catastrophe losses excluding losses related to the Company's external reinsurance assumed lines except for Hurricane Isaac, the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods, the 2011 and 2012 tornadoes and other severe storms in the U.S. including Superstorm Sandy. 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, 2012 and September 30, 2011.

3 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 and certain other run off.

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, 2012 was 97.6% and 97.1%, decreases of 0.8 points and 0.5 points from the same periods in 2011. The claims and claim adjustment expense ratio for both periods reflects decreased current accident year loss ratios in most lines of business and a greater mix of personal lines, partially offset by increased surety losses. The increases in the underwriting expense ratio in both periods reflect increased investment in growth-related items, primarily captive sales representatives and advertising, increased variable compensation due to improved operating results, higher benefit costs, and increased investment in technology, partially offset by earned premium growth and higher servicing carrier revenue.

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, 2012 was 112.9% and 104.7%, an increase of 8.7 points and a decrease of 2.8 points versus the same periods in 2011. Both periods were impacted by higher unfavorable net losses attributable to prior years, primarily pre-2011 workers compensation business and LIU third party. The increase in the quarter primarily reflects an increase in catastrophe losses primarily related to Superstorm Sandy partially offset by the changes in the combined ratio previously discussed and lower losses associated with re-estimation of the current accident year. The decrease in the year reflects lower catastrophes losses and prior year development for asbestos reserves recorded in 2011 partially offset by the changes in the combined ratio previously discussed.

PERSONAL INSURANCE

Overview – Personal Insurance

Personal Insurance sells automobile, homeowners and other types of property and casualty insurance coverage, as well as life and annuity products, to individuals and insurance companies in the United States. Personal Insurance is composed of two market segments: Personal Lines (including Individual Life) and Safeco. Personal Lines products are distributed through more than 2,400 licensed captive sales representatives, approximately 500 licensed telesales counselors, third-party producers (including banks for life products) and the Internet. Personal Lines' largest source of new business is through its over 14,000 sponsored affinity groups (including employers, professional and alumni associations, credit unions, and other partnerships). Safeco products are distributed nationally through independent agents.

Effective in the third quarter of 2012, Personal Insurance became a new SBU replacing the former Personal Markets SBU. The financial results of Personal Insurance differ from Personal Markets results principally due to the addition of Safeco. As such, results of Personal Insurance are not directly comparable to the previously reported financial information for Personal Markets. All prior periods have been restated to reflect this change.

Personal Insurance NWP by market segment was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Personal Lines	$1,985	$1,799	10.3%	$8,103	$7,378	9.8%
Safeco	1,533	1,394	10.0	5,807	5,330	8.9
Total NWP	$3,518	$3,193	10.2%	$13,910	$12,708	9.5%

Personal Insurance NWP by line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Private passenger automobile	$2,095	$1,926	8.8%	$8,303	$7,713	7.6%
Homeowners and other	1,298	1,145	13.4	5,202	4,637	12.2
Individual life	125	122	2.5	405	358	13.1
Total NWP	$3,518	$3,193	10.2%	$13,910	$12,708	9.5%

NWP for the three and twelve months ended December 31, 2012 was $3.518 billion and $13.910 billion, respectively, increases of $325 million and $1.202 billion over the same periods in 2011.

Private passenger automobile NWP for the three and twelve months ended December 31, 2012 was $2.095 billion and $8.303 billion, respectively, increases of $169 million and $590 million over the same periods in 2011. The increases reflect 5.3% growth in auto policies in-force as compared to December 31, 2011 as well as rate increases.

Homeowners and other NWP for the three and twelve months ended December 31, 2012 was $1.298 billion and $5.202 billion, respectively, increases of $153 million and $565 million over the same periods in 2011. The increases reflect 6.7% growth in homeowners policies in-force as compared to December 31, 2011 as well as rate increases.

Individual life NWP for the three and twelve months ended December 31, 2012 was $125 million and $405 million, respectively, increases of $3 million and $47 million over the same periods in 2011. The increase in the year was driven by increased sales across all channels, primarily structured settlements.

Results of Operations – Personal Insurance

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Revenues	$3,805	$3,498	8.8%	$14,530	$13,457	8.0%
PTOI before catastrophes and net incurred losses attributable to prior years	$539	$403	33.7%	$2,202	$1,857	18.6%
Catastrophes[1]	(553)	(136)	NM	(1,346)	(1,765)	(23.7)
Net incurred losses attributable to prior years	6	55	(89.1)	154	178	(13.5)
Pre-tax operating (loss) income	($8)	$322	NM	$1,010	$270	NM

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

NM=Not Meaningful

Pre-tax operating (loss) income for the three and twelve months ended December 31, 2012 was ($8) million and $1.010 billion, respectively, versus $322 million and $270 million in the same periods in 2011. Both periods benefitted from higher net earned premium, higher net investment income and favorable non-catastrophe loss trends across all lines of business. Catastrophe losses were higher in the quarter, principally driven by Superstorm Sandy, but catastrophe losses for the full year were lower than the prior year.

Revenues for the three and twelve months ended December 31, 2012 were $3.805 billion and $14.530 billion, respectively, increases of $307 million and $1.073 billion over the same periods in 2011. 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, 2012 was $3.472 billion and $13.215 billion, respectively, increases of $289 million and $1.011 billion over the same periods in 2011. The increases in both periods reflect the premium earned associated with the changes in NWP previously discussed.

Net investment income for the three and twelve months ended December 31, 2012 was $276 million and $1.079 billion, respectively, increases of $13 million and $43 million over the same periods in 2011. The increases were driven by a higher invested asset base due to the reinvestment of cash flow from operations partially offset by a lower yield environment.

Claims, benefits and expenses for the three and twelve months ended December 31, 2012 were $3.813 billion and $13.516 billion, respectively, increases of $636 million and $334 million over the same periods in 2011. Both periods experienced an increase in claims and expenses consistent with business growth which was partially offset by favorable non-catastrophe loss trends across all lines of business. The increase in the quarter was also driven by higher catastrophe losses, primarily Superstorm Sandy, but full year catastrophe losses were lower than the prior year. The increase in the year was also driven by an increase in higher variable compensation costs due to improved earnings.

PERSONAL INSURANCE	Three Months Ended December 31, 2012	2011	Change (Points)	Twelve Months Ended December 31, 2012	2011	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	62.9%	65.8%	(2.9)	61.7%	63.6%	(1.9)
Underwriting expense ratio	25.5	25.9	(0.4)	25.8	25.6	0.2
Subtotal	88.4	91.7	(3.3)	87.5	89.2	(1.7)
Catastrophes[1]	16.6	4.4	12.2	10.5	14.9	(4.4)
Net incurred losses attributable to prior years	(0.2)	(1.8)	1.6	(1.2)	(1.5)	0.3
Total combined ratio	104.8%	94.3%	10.5	96.8%	102.6%	(5.8)

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

The Personal Insurance combined ratio before catastrophes and net incurred losses attributable to prior years for the three and twelve months ended December 31, 2012 was 88.4% and 87.5%, respectively, decreases of 3.3 points and 1.7 points from the same periods in 2011. Decreases in the claims and claim adjustment expense ratio in both periods primarily reflect favorable non-catastrophe loss trends across all lines of business as well as the impact of rate increases. The decrease in the underwriting expense ratio for the quarter is primarily a result of premium rate increases and lower advertising costs. The increase in the underwriting expense ratio for the year is primarily the result of an investment in information technology and growth-related items, such as increased captive sales representatives and higher advertising expenditures, as well as higher variable compensation costs due to improved earnings, partially offset by the impact of premium rate increases.

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, 2012 was 104.8% and 96.8%, respectively, an increase of 10.5 points and a decrease of 5.8 points versus the same periods in 2011. The increase in the quarter is primarily driven by increased catastrophe losses, partially offset by the changes in the combined ratio previously discussed. The decrease in the year is due to lower catastrophe losses and the changes in the combined ratio previously discussed. Both periods were impacted by lower favorable incurred losses attributable to prior years.

COMMERCIAL INSURANCE

Overview – Commercial Insurance

Commercial Insurance offers a wide array of property-casualty and group benefits insurance coverages through independent agents, brokers and benefit consultants throughout the United States. Commercial Insurance is organized into the following market segments: Business Insurance, National Insurance, Group Benefits, and Other Commercial Insurance. Business Insurance serves the small and middle market customer through a regional operating model that combines local underwriting, market knowledge and service orientation with the scale advantages of a national company. National Insurance provides commercial lines products and services, including third-party administration, to large businesses. Group Benefits provides mid-sized and large businesses with short- and long-term disability insurance products and group life insurance. Other Commercial Insurance primarily consists of internal reinsurance and assumed business from state based workers compensation involuntary market pools. The Company is also a servicing carrier for state based workers compensation involuntary market pools.

Effective in the third quarter of 2012, Commercial Insurance was formed by combining the Regional Companies Group, which was previously part of the Liberty Mutual Agency Corporation ("LMAC") strategic business unit, and the Commercial Markets strategic business unit, excluding LMR, which is now part of Global Specialty. All prior periods have been restated to reflect the realignment.

Commercial Insurance NWP by market segment was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Business Insurance	$1,397	$1,506	(7.2%)	$6,269	$6,487	(3.4%)
National Insurance	574	524	9.5	2,452	2,312	6.1
Group Benefits	197	192	2.6	787	787	-
Other Commercial Insurance	57	44	29.5	228	233	(2.1)
Total NWP	$2,225	$2,266	(1.8%)	$9,736	$9,819	(0.8%)

Commercial Insurance NWP by line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Workers compensation - Voluntary	$752	$779	(3.5%)	$3,532	$3,669	(3.7%)
Workers compensation - Involuntary	34	19	78.9	136	82	65.9
Commercial automobile	343	349	(1.7)	1,453	1,480	(1.8)
Commercial multiple-peril	485	500	(3.0)	2,051	2,081	(1.4)
General liability	245	276	(11.2)	1,046	1,077	(2.9)
Group disability and life	197	192	2.6	787	787	-
Other Lines	169	151	11.9	731	643	13.7
Total NWP	$2,225	$2,266	(1.8%)	$9,736	$9,819	(0.8%)

NWP for the three and twelve months ended December 31, 2012 was $2.225 billion and $9.736 billion, respectively, decreases of $41 million and $83 million from the same periods in 2011. Both periods reflect a decline in new business premium within Business Insurance due to disciplined underwriting in a continued competitive marketplace and a large general liability account written in 2011, partially offset by

increased rate and exposures on renewal business across all property and casualty lines of business, increased audit premium, and higher involuntary market premium due to pool growth. Both periods also reflect a reduction in workers compensation exposures, partially offset by increasing rate and audit premium. The year was further impacted by two large 2011 events which did not recur, a multi-year policy written in 2011 and a large disability account transfer in Group Benefits.

Results of Operations – Commercial Insurance

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Revenues	$2,885	$2,835	1.8%	$11,376	$11,156	2.0%
PTOI before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation	$208	$173	20.2%	$664	$518	28.2%
Catastrophes[1]	(218)	(22)	NM	(517)	(688)	(24.9)
Net incurred losses attributable to prior years[2]	28	42	(33.3)	117	57	105.3
Current accident year re-estimation[3]	(21)	(120)	(82.5)	-	-	-
Pre-tax operating (loss) income	($3)	$73	NM	$264	($113)	NM

1 Catastrophes include all current and prior accident year catastrophe losses. 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 $2 million and $42 million for the three and twelve months ended December 31, 2012 and ($35) million and ($29) million for the same periods in 2011. Net of amortization of deferred (losses) gains on assumed retroactive reinsurance of ($2) million and zero for the three and twelve months ended December 31, 2012 and zero and $5 million for the same periods in 2011.

3 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2012 and September 30, 2011.

NM = Not Meaningful

Pre-tax operating (loss) income for the three and twelve months ended December 31, 2012 was ($3) million and $264 million, respectively, versus $73 million and ($113) million in the same periods in 2011. Both periods were favorably impacted by decreased current accident year losses in the workers compensation, commercial multiple-peril and commercial auto lines of business partially offset by higher variable compensation costs. The decrease in the quarter reflects higher catastrophe losses primarily due to Superstorm Sandy. The year was favorably impacted by lower catastrophe losses and favorable net incurred losses attributable to prior years.

Revenues for the three and twelve months ended December 31, 2012 were $2.885 billion and $11.376 billion, respectively, increases of $50 million and $220 million over the same periods in 2011. The major components of revenues are net premium earned, net investment income and fee and other revenues.

Net premium earned for the three and twelve months ended December 31, 2012 was $2.481 billion and $9.772 billion, respectively, increases of $37 million and $186 million over the same periods in 2011. The increases in both periods reflect significant rate increases across all lines of business, higher involuntary market premium primarily due to pool growth, higher audit premiums and increased National Insurance net written premium.

Net investment income for the three and twelve months ended December 31, 2012 was $320 million and $1.281 billion, respectively, representing no change and an increase of $1 million versus the same periods in 2011.

Fee and other revenues for the three and twelve months ended December 31, 2012 were $84 million and $323 million, respectively, increases of $13 million and $33 million over the same periods in 2011. The increases in both periods reflect higher commission revenue from servicing carrier operations due to higher involuntary market premium volume, and third-party administrator fee income. 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, 2012 were $2.888 billion and $11.112 billion, respectively, an increase of $126 million and a decrease of $157 million versus the same periods in 2011. The increase in the quarter reflects higher catastrophe losses primarily due to Superstorm Sandy. Both periods were impacted by decreased current accident year losses in the workers compensation, commercial multiple-peril and commercial auto lines of business partially offset by higher variable compensation costs. The year was favorably impacted by lower catastrophe losses and favorable net incurred losses attributable to prior years.

	Three Months Ended December 31,			Twelve Months Ended December 31,		
			Change			Change
COMMERCIAL INSURANCE	**2012**	**2011**	**(Points)**	**2012**	**2011**	**(Points)**
Combined ratio before catastrophes, net incurred losses attributable to prior years and current accident year re-estimation						
Claims and claim adjustment expense ratio	75.7%	79.0%	(3.3)	77.6%	79.0%	(1.4)
Underwriting expense ratio	28.1	27.1	1.0	28.5	28.7	(0.2)
Dividend ratio	0.3	0.5	(0.2)	0.4	0.4	-
Subtotal	104.1	106.6	(2.5)	106.5	108.1	(1.6)
Catastrophes[1]	9.6	1.0	8.6	5.8	7.8	(2.0)
Net incurred losses attributable to prior years[2]	(1.2)	(1.7)	0.5	(1.3)	(0.6)	(0.7)
Current accident year re-estimation[3]	0.9	5.2	(4.3)	-	-	-
Total combined ratio	113.4%	111.1%	2.3	111.0%	115.3%	(4.3)

1 Catastrophes include all current and prior accident year catastrophe losses. 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.
3 Re-estimation of the current accident year loss reserves for the nine months ended September 30, 2012 and September 30, 2011.

The Commercial Insurance 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, 2012 was 104.1% and 106.5%, respectively, decreases of 2.5 points and 1.6 points from the same periods in 2011. The claims and claim adjustment expense ratio in both periods was impacted by decreased workers compensation, commercial multiple-peril and commercial auto losses. The underwriting expense ratio increased 1.0 points in the quarter and decreased 0.2 points for the year. The quarter reflects higher variable compensation costs. The year reflects higher 2012 earned premium partially offset by higher 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, 2012 was 113.4% and 111.0%, respectively, an increase of 2.3 points and a decrease of 4.3 points versus the same periods in 2011. The increase in the quarter reflects higher catastrophe losses attributable to Superstorm Sandy and lower favorable net incurred losses attributable to prior years, partially offset by lower losses associated with re-estimation of the current accident year. The decrease in the year reflects the severe tornado and severe storm losses incurred during 2011 and favorable net incurred losses attributable to prior years during 2012.

LIBERTY INTERNATIONAL

Overview – Liberty International

Liberty International sells property, casualty, health and life insurance products and services to individuals and businesses in three geographic regions: Latin America, including Venezuela, Brazil, Colombia, Argentina (Liberty ART S.A., a workers compensation business, was sold in June 2012. Liberty Seguros Argentina S.A. remains.), Chile and Ecuador (as a result of the Panamericana de Seguros del Ecuador S.A. and Cervantes S.A. Compania de Seguros y Reaseguros acquisitions in August 2012); Europe, including Spain, Portugal, Turkey, Poland, Ireland (as a result of the Quinn Insurance Limited - "QIL" - acquisition in November 2011), United Kingdom (as a result of exercising renewal rights option over the Great Britain and Northern Ireland portfolios of QIL) and Russia (as a result of the KIT Finance Insurance acquisition in March 2012); and Asia, including Thailand, Singapore, China (including Hong Kong) and Vietnam. Private passenger automobile insurance is the single largest line of business.

The International SBU was realigned effective in the third quarter of 2012. The financial results differ principally due to the removal of the results of operation of LIU, including its Syndicate 4472. As such, the results of Liberty International are not directly comparable to the previously reported financial information for the International SBU. All prior periods have been restated to reflect this change.

Liberty International NWP by market segment was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Latin America	$1,086	$978	11.0%	$3,795	$3,542	7.1%
Europe	417	352	18.5	1,510	1,314	14.9
Asia	122	94	29.8	442	377	17.2
Total NWP	$1,625	$1,424	14.1%	$5,747	$5,233	9.8%
Foreign exchange effect on growth			(2.8%)			(5.7%)
NWP growth excluding foreign exchange			16.9%			15.5%

Liberty International NWP by line of business was as follows:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Private passenger automobile	$965	$862	11.9%	$3,356	$3,132	7.2%
Commercial automobile	131	82	59.8	433	314	37.9
Homeowners	67	59	13.6	239	215	11.2
Life and health	238	197	20.8	858	723	18.7
Other commercial[1]	224	224	-	861	849	1.4
Total NWP	$1,625	$1,424	14.1%	$5,747	$5,233	9.8%

1 Premium related to other commercial lines including bonds, workers compensation, property and fire, small and medium enterprise and marine and cargo lines of business.

NWP for the three and twelve months ended December 31, 2012 was $1.625 billion and $5.747 billion, respectively, increases of $201 million and $514 million over the same periods in 2011. The increases in both periods reflect organic growth across all the regions, primarily in Latin America, due to the impact of inflation in Venezuela, followed by Europe, mainly attributable to the acquisitions in Ireland (primarily in the private passenger auto line of business) and Russia, and to a lesser extent Asia, led by China. The increases were partially offset by the impact of foreign exchange (approximately $40 million in the quarter and $297 million in the year, primarily driven by a weakened Brazilian real and euro).

Results of Operations – Liberty International

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Revenues	$1,570	$1,432	9.6%	$6,019	$5,478	9.9%
PTOI before catastrophes and net incurred losses attributable to prior years	$78	$75	4.0%	$266	$288	(7.6%)
Catastrophes[1]	7	(26)	NM	7	(26)	NM
Net incurred losses attributable to prior years[2]	1	(42)	NM	(14)	(58)	(75.9)
PTOI	$86	$7	NM	$259	$204	27.0%

1 Catastrophes include all current and prior accident year catastrophe losses. 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 and ($1) million for the three months and twelve months ended December 31, 2012, respectively, and ($6) million for the same periods in 2011.
NM = Not Meaningful

PTOI for the three and twelve months ended December 31, 2012 was $86 million and $259 million, respectively, increases of $79 million and $55 million over the same periods in 2011. The increases in both periods were primarily driven by favorable catastrophe loss development in 2012 related to Thailand floods of 2011 and favorable net incurred losses attributable to prior years compared to 2011, partially offset by restructuring cost in Ireland in 2012. The increase in the year was partially offset by an increase in expenses in 2012 related to enhancements to global technology infrastructure. Foreign exchange impact contributed to the increase in the quarter (approximately $4 million) but partially offset the increase in the year (approximately $4 million).

Revenues for the three and twelve months ended December 31, 2012 were $1.570 billion and $6.019 billion, respectively, increases of $138 million and $541 million over the same periods in 2011. 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, 2012 was $1.410 billion and $5.390 billion, respectively, increases of $137 million and $446 million over the same periods in 2011. The increases in both periods reflect the previously mentioned growth in NWP in 2012, partially offset by the impact of foreign exchange.

Net investment income for the three and twelve months ended December 31, 2012 was $111 million and $445 million, respectively, increases of $8 million and $50 million over the same periods in 2011. The increases in both periods reflect the 2011 and 2012 acquisitions (primarily Ireland), higher investment income in Venezuela, primarily due to higher investment yields, and a higher invested asset base due to the reinvestment of cash flow from operations driven by the growth in net written premium. The increases were partially offset by a decrease in overall investment yields due to lower reinvestment rates, primarily in Europe and Brazil.

Claims, benefits and expenses for the three and twelve months ended December 31, 2012 were $1.481 billion and $5.743 billion, respectively, increases of $67 million and $458 million over the same periods in 2011. The increases in both periods reflect the organic growth in Latin America led by Venezuela primarily due to inflation, as well as the acquisitions in Ireland, and to a lesser extent, Russia and Ecuador, partially offset by favorable catastrophe loss development in 2012 related to Thailand floods of 2011 and favorable net incurred losses attributable to prior years compared to 2011.

	Three Months Ended December 31,			Twelve Months Ended December 31,		
LIBERTY INTERNATIONAL	2012	2011	Change (Points)	2012	2011	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	64.1%	66.0%	(1.9)	66.1%	66.0%	0.1
Underwriting expense ratio	38.4	37.0	1.4	37.0	35.5	1.5
Subtotal	102.5	103.0	(0.5)	103.1	101.5	1.6
Catastrophes[1]	(0.5)	2.1	(2.6)	(0.1)	0.5	(0.6)
Net incurred losses attributable to prior years	-	3.3	(3.3)	0.2	1.2	(1.0)
Total combined ratio	102.0%	108.4%	(6.4)	103.2%	103.2%	-

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

The combined ratio before catastrophes and net incurred losses attributable to prior years for the three and twelve months ended December 31, 2012 was 102.5% and 103.1%, respectively, a decrease of 0.5 points in the quarter and an increase of 1.6 points in the year. The decrease in claims and claims adjustment expense ratio in the quarter was primarily driven by select countries in Latin America, led by Brazil, partially offset by an increase in underwriting expense ratio primarily driven by the addition of Ireland, including the restructuring cost (0.8 points). The increase in the year was primarily driven by higher underwriting expense ratio mainly related to investments in global technology infrastructure, as well as the impact of the acquisition in Ireland including the restructuring cost (0.2 points).

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, 2012 was 102.0% and 103.2%, respectively, a decrease of 6.4 points in the quarter and no change in the year. The total combined ratios reflect the changes in the combined ratio previously discussed, as well as favorable catastrophe loss development related to the 2011 Thailand floods and lower incurred losses attributable to prior years as compared to the same periods in 2011.

GLOBAL SPECIALTY

Overview – Global Specialty

Global Specialty is composed of a wide array of products and services offered through three market segments: LIU, LMS, and LMR. LIU, which sells specialty commercial insurance and reinsurance worldwide, 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 Syndicate 4472, also provides multi-line insurance and reinsurance worldwide written through the Lloyds' platform. LMS is a leading provider of nationwide contract and commercial surety bonds to businesses of all sizes. LMR provides reinsurance to domestic and foreign insurance and reinsurance companies.

The Global Specialty SBU was formed during the third quarter of 2012. The SBU is the sum of: LIU (including Syndicate 4472), formerly part of International; LMS, formerly part of LMAC and LMR, formerly part of Commercial Markets. All prior periods have been restated to reflect this change.

Global Specialty NWP by market segment was as follow:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
LIU	$723	$682	6.0%	$3,235	$2,976	8.7%
LMS	170	170	-	718	741	(3.1)
LMR	79	83	(4.8)	357	316	13.0
Total NWP	$972	$935	4.0%	$4,310	$4,033	6.9%
Foreign exchange effect on growth			0.3%			(0.9%)
NWP growth excluding foreign exchange			3.7%			7.8%

Global Specialty's major product lines are as follows:

1. Syndicate 4472: multi-line insurance and reinsurance with an emphasis on property, contingent lines, marine reinsurance and property and casualty reinsurance;
2. LIU inland marine program: handset protection coverage for lost or damaged devices;
3. LIU third party: includes casualty, excess casualty, directors and officers, errors and omissions, environmental impairment liability, commercial automobile, railroad and other;
4. LIU first party: includes marine, energy, construction, aviation and property;
5. LIU other: includes workers compensation, surety, trade credit, excess and surplus property and crisis management;
6. LMS: includes contract and commercial surety bonds; and
7. LMR: reinsurance through both domestic and foreign insurance and reinsurance companies.

Global Specialty NWP by line of business was as follow:

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	2012	2011	Change	2012	2011	Change
Syndicate 4472	$250	$266	(6.0%)	$1,439	$1,382	4.1%
LIU inland marine program	146	106	37.7	522	405	28.9
LIU third party	221	207	6.8	872	806	8.2
LIU first party	90	85	5.9	323	314	2.9
LIU other	16	18	(11.1)	79	69	14.5
LMS	170	170	-	718	741	(3.1)
LMR	79	83	(4.8)	357	316	13.0
Total NWP	$972	$935	4.0%	$4,310	$4,033	6.9%

NWP for the three and twelve months ended December 31, 2012 was $972 million and $4.310 billion, respectively, increases of $37 million and $277 million over the same periods in 2011. The increase in both periods reflect growth driven by the LIU inland marine business due to subscriber growth, pricing mix and the inception of a program in Japan in 2012 which contributed $62 million for the year. For the twelve months ended December 31, 2012, growth was also driven by LMR as a result of price increases and higher line sizes on existing contracts, and LIU third party and Syndicate 4472 due to favorable rates and new business. The increase for the year was partially offset by a decline in Surety lines premium largely due to a decline in the volume of bonded construction projects.

Results of Operations – Global Specialty

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	2012	2011	Change	2012	2011	Change
Revenues	$1,242	$1,203	3.2%	$4,607	$4,224	9.1%
PTOI before catastrophes and net incurred losses attributable to prior years	$92	$191	(51.8%)	$617	$713	(13.5%)
Catastrophes [1]	(144)	(70)	105.7	(140)	(415)	(66.3)
Net incurred losses attributable to prior years [2]	(112)	(58)	93.1	(100)	151	NM
Pre-tax operating (loss) income	($164)	$63	NM	$377	$449	(16.0%)

1 Catastrophes include all current and prior accident year catastrophe losses excluding losses related to the Company's external reinsurance assumed lines except for Hurricane Isaac, the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods, the 2011 and 2012 tornadoes and other severe storms in the U.S. including Superstorm Sandy. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of $1 million and $15 million for the three months and twelve months ended December 31, 2012 and zero and $17 million for the same periods in 2011.

NM = Not Meaningful

Pre-tax operating (loss) income for the three and twelve months ended December 31, 2012 was ($164) million and $377 million, respectively, versus $63 million and $449 million in the same periods in 2011. The decrease in both periods was impacted by current year accident losses in LMS and unfavorable net incurred losses attributable to prior years for LIU third party. The quarter was also impacted by unfavorable catastrophe losses for Syndicate 4472 and LMR due to Superstorm Sandy. Impacting the year was lower favorable net incurred losses attributable to prior years within Syndicate 4472 offset with favorable catastrophes incurred in 2012 compared to 2011.

Revenues for the three and twelve months ended December 31, 2012 were $1.242 billion and $4.607 billion, respectively, increases of $39 million and $383 million over the same periods in 2011. 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, 2012 was $1.133 billion and $4.205 billion, respectively, increases of $20 million and $324 million over the same periods in 2011. The increases in both periods reflect the previously mentioned growth in NWP.

Net investment income for the three and twelve months ended December 31, 2012 was $86 million and $339 million, respectively, increases of $1 million and $12 million over the same periods in 2011. The increases in both periods reflect a higher invested asset base due to the reinvestment of cash flow from operations driven by the growth in NWP, partially offset by lower investment yields.

Claims, benefits and expenses for the three and twelve months ended December 31, 2012 were $1.385 billion and $4.175 billion, respectively, increases of $248 million and $411 million over the same periods in 2011. The increase for both periods was primarily driven by the growth of the LIU inland marine program as well as current year accident losses incurred for LMS and unfavorable incurred losses attributable to prior years for LIU third party. The quarter was also impacted by unfavorable catastrophe losses for Syndicate 4472 and LMR due to Superstorm Sandy. Impacting the year was lower favorable net incurred losses attributable to prior years within Syndicate 4472 partially offset by lower catastrophe losses (primarily within Syndicate 4472 business) in 2012 as compared to the catastrophe losses related to the Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene and the tornadoes and other severe storms in the U.S. in 2011.

	Three Months Ended December 31,			**Twelve Months Ended December 31,**		
GLOBAL SPECIALTY	**2012**	**2011**	**Change (Points)**	**2012**	**2011**	**Change (Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	70.2%	61.8%	8.4	63.7%	60.3%	3.4
Underwriting expense ratio	28.5	27.8	0.7	28.8	29.0	(0.2)
Dividend ratio	0.2	0.2	-	0.2	0.2	-
Subtotal	98.9	89.8	9.1	92.7	89.5	3.2
Catastrophes [1]	12.6	6.3	6.3	3.3	10.8	(7.5)
Net incurred losses attributable to prior years	10.0	5.2	4.8	2.4	(4.0)	6.4
Total combined ratio	121.5%	101.3%	20.2	98.4%	96.3%	2.1

1 Catastrophes include all current and prior accident year catastrophe losses excluding losses related to the Company's external reinsurance assumed lines except for Hurricane Isaac, the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods, the 2011 and 2012 tornadoes and other severe storms in the U.S. including Superstorm Sandy. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

The Global Specialty combined ratio before catastrophes and net incurred losses attributable to prior years for the three and twelve months ended December 31, 2012 was 98.9% and 92.7%, respectively, increases of 9.1 points and 3.2 points over the same periods in 2011. The increases in both periods were attributable to higher losses in LMS and LIU third party. In the quarter, the increase in the underwriting expense ratio was driven by lower earned premium in Syndicate 4472, due to favorable prior year signing adjustments and LMS earned premium. The lower underwriting expense ratio in the year was driven by increased scale and efficiencies of the business.

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, 2012 was 121.5% and 98.4%, respectively, increases of 20.2 and 2.1 points over the same periods in 2011. The increase in the quarter reflects the changes to the combined ratio discussed above, unfavorable LIU third party net incurred losses attributable

to prior years, and increased catastrophe losses related to Superstorm Sandy. The increase in the year also reflects 2012 unfavorable incurred losses attributable to prior years offset by net favorable catastrophe losses incurred in 2012 compared to the catastrophe losses related to the Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene and the tornadoes and other severe storms in the U.S. 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 Commercial Insurance 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") and Liberty Re annuity business.

- Effective July 1, 2011, Corporate and Commercial Insurance 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 Insurance 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 Insurance 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 Insurance reports its discount based on statutory discount rates. Corporate and Other results reflect the difference between the statutory and risk-free rate.

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

- For presentation in this MD&A, 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.

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

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

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

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Reinsurance, net	$74	($143)	NM	($214)	($497)	(56.9%)
Workers compensation[1]	76	33	130.3	65	(104)	NM
Other	1	-	NM	1	3	(66.7)
Total NWP	$151	($110)	NM	($148)	($598)	(75.3%)

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

NWP for the three and twelve months ended December 31, 2012 was $151 million and ($148) million, respectively, increases of $261 million and $450 million over the same periods in 2011. The increases were primarily due to an increase in assumed premium related to the Company's internal reinsurance program, a decrease in ceded premium related to the homeowners quota share treaty covering Personal Insurance homeowners due to a change in terms, effective December 31, 2012, and a decrease in the Company's workers compensation "booked as billed" adjustment.

Results of Operations – Corporate and Other

	Three Months Ended December 31,			Twelve Months Ended December 31,		
$ in Millions	**2012**	**2011**	**Change**	**2012**	**2011**	**Change**
Revenues	$126	($5)	NM	$412	$356	15.7%
Pre-tax operating loss before catastrophes, net incurred losses attributable to prior years and LP and LLC income	($358)	($248)	44.4%	($1,168)	($918)	27.2%
Catastrophes[1]	65	20	NM	136	213	(36.2)
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	2	(10)	NM	(56)	(351)	(84.0)
- All other[3]	(242)	(71)	NM	(471)	(99)	NM
Pre-tax operating loss before LP and LLC income	(533)	(309)	72.5	(1,559)	(1,155)	35.0
LP and LLC income [4]	99	107	(7.5)	353	583	(39.5)
Pre-tax operating loss	($434)	($202)	114.9%	($1,206)	($572)	110.8%

1 Catastrophes include all current and prior accident year catastrophe losses incurred excluding losses related to the Company's external reinsurance assumed lines except for Hurricane Isaac, the 2011 Australia floods, Cyclone Yasi, Japan earthquake and tsunami, New Zealand earthquakes, Hurricane Irene, Thailand floods, the 2011 and 2012 tornadoes and other severe storms in the U.S. including Superstorm Sandy. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.
2 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 zero and ($1) million for the three and twelve months December 31, 2012 and zero and ($8) million for the same periods in 2011. Net of amortization of deferred (losses) gains on retroactive reinsurance of ($1) million and $29 million for the three and twelve months ended December 31, 2012 and $5 million and $129 million for the same periods in 2011. 2011 reflects a gain on commutation of two retroactive reinsurance contracts during the first quarter.
4 LP and LLC income is included in net investment income in the accompanying consolidated statements of income.
NM = Not Meaningful

Pre-tax operating loss for the three and twelve months ended December 31, 2012 was $434 million and $1.206 billion, respectively, increases (in the loss) of $232 million and $634 million over the same periods in 2011. Both periods were impacted by unfavorable prior year loss development related to pre-2011 workers compensation business assumed from Commercial Insurance, additional unallocated loss adjustment expense reserves, unfavorable annuity reserve development and higher corporate expenses as a result of improved profitability and a lower pension discount rate. The quarter is also driven by higher losses related to Corporate's internal reinsurance program as a result of Superstorm Sandy, partially offset

by an increase in ceded losses related to the homeowners quota share treaty. The change in the year is also driven by lower valuation increases in LP and LLC investments, a gain on the commutation of the workers compensation retroactive reinsurance agreement in 2011, and an increase in ceded earned premium associated with the homeowners quota share treaty, partially offset by higher asbestos and environmental reserves in 2011.

Revenues for the three and twelve months ended December 31, 2012 were $126 million and $412 million, respectively, increases of $131 million and $56 million over the same periods in 2011. The major components of revenues are net premium earned, net investment income, net realized gains, and fee and other revenues.

Net premium earned for the three and twelve months ended December 31, 2012 was ($107) million and ($417) million, respectively, increases of $19 million and $79 million over the same periods in 2011. The increases reflect the earned premium associated with the changes in reinsurance NWP previously discussed, excluding the homeowners quota share treaty. The change in terms for the homeowners quota share treaty had no impact to earned premium.

Net investment income for the three and twelve months ended December 31, 2012 was ($5) million and $93 million, respectively, decreases of $87 million and $392 million from the same periods in 2011. The decrease in the year and to a lesser extent in the quarter reflects lower valuation increases in LP and LLC investments. In addition, both periods reflect a decrease in taxable interest income due to lower investment yields primarily attributable to a tactical portfolio realignment.

Net realized gains for the three and twelve months ended December 31, 2012 were $161 million and $458 million, respectively, increases of $184 million and $305 million over the same periods in 2011. The increases in both periods primarily relate to gains recognized from security sales as part of a tactical portfolio realignment and gains on the sale of investments in the energy sector. The increase in the year was also impacted by contingent consideration recognized in connection with the prior sale of certain Commercial Insurance policy renewal rights in 2009, partially offset by increased impairments due to market volatility.

Fee and other revenues for the three and twelve months ended December 31, 2012 were $77 million and $278 million, increases of $15 million and $64 million over the same periods in 2011. The increases primarily reflect higher oil and gas revenues due to increased production.

Claims, benefits and expenses for the three and twelve months ended December 31, 2012 were $399 million and $1.160 billion, respectively, increases of $179 million and $385 million over the same periods in 2011. Both periods were impacted by higher corporate expenses primarily due to employee benefits, unfavorable prior year loss development related to pre-2011 workers compensation business assumed from Commercial Insurance, an increase in assumed losses related to internal reinsurance programs growth and Superstorm Sandy, additional unallocated loss adjustment expense reserves, unfavorable annuity reserve development, and higher depreciation charges related to Liberty Energy. The increase in the quarter is partially offset by an increase in ceded losses associated with the homeowners quota share treaty due to Superstorm Sandy. The change in the year is also driven by a gain on the commutation of the workers compensation retroactive reinsurance agreement in 2011, partially offset higher asbestos and environmental reserves in 2011 and a decrease in interest expense as a result of debt repurchases.

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, 2012 and December 31, 2011:

$ in Millions	**As of December 30, 2012**		**As of December 31, 2011**	
Invested Assets by Type	**Carrying Value**	**% of Total**	**Carrying Value**	**% of Total**
Fixed maturities, available for sale, at fair value	$64,094	82.1%	$60,576	82.2%
Equity securities, available for sale, at fair value	2,495	3.2	1,954	2.7
LPs and LLCs	3,767	4.8	3,389	4.6
Commercial mortgage loans	1,335	1.7	1,196	1.6
Short-term investments	208	0.3	201	0.3
Other investments	677	0.9	400	0.5
Cash and cash equivalents	5,484	7.0	5,972	8.1
Total invested assets	$78,060	100.0%	$73,688	100.0%

Total invested assets as of December 31, 2012 were $78.060 billion, an increase of $4.372 billion or 5.9% over December 31, 2011. The increase reflects an increase in unrealized gains related to decreases in interest rates, positive equity market performance, and the reinvestment of cash flow from operations.

Fixed maturities as of December 31, 2012 were $64.094 billion, an increase of $3.518 billion or 5.8% over December 31, 2011. The increase reflects investment of cash associated with the QIL acquisition, an increase in unrealized gains related to decreases in interest rates, and the reinvestment of cash flow from operations. As of December 31, 2012, included in fixed maturities are commitments to purchase various residential mortgage-backed securities at a cost and fair value of $13 million and various corporate and municipal securities at a cost and fair value of $141 million.

Equity securities available for sale as of December 31, 2012 were $2.495 billion ($2.097 billion common stock and $398 million preferred stock) versus $1.954 billion as of December 31, 2011 ($1.608 billion common stock and $346 million preferred stock), an increase of $541 million or 27.7% over December 31,

2011. Of the $2.097 billion of common stock at December 31, 2012, $315 million relates to securities associated with non-guaranteed unit linked products where the policyholder bears the investment risk. The increase in total equity securities available for sale was consistent with the Company's continued investment in this asset class as well as broader equity market performance.

Investments in LPs and LLCs as of December 31, 2012 were $3.767 billion, an increase of $378 million or 11.2% over December 31, 2011. These investments consist of traditional private equity partnerships of $2.050 billion, other partnerships (primarily energy) of $1.106 billion, and real estate partnerships of $611 million. The increase reflects improved 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, 2012, the Company had unfunded commitments in traditional private equity partnerships, real estate, natural resources, and other of $824 million, $253 million, $1.168 billion, and $257 million, respectively.

Commercial mortgage loans as of December 31, 2012 were $1.335 billion (net of $22 million of loan loss reserves or 1.6% of the outstanding loan portfolio), an increase of $139 million or 11.6% over December 31, 2011. The increase primarily reflects a $235 million increase in loans, partially offset by $92 million in principal repayments and an increase of $4 million to the loan loss reserve. The entire commercial loan portfolio is U.S. based. As of December 31, 2012, the average total loan size was $1 million and the average loan participation size was less than $1 million. The number of loans in the portfolio increased from 3,272 at December 31, 2011 to 3,679 at December 31, 2012. Approximately 93% of the loans are full or partial recourse to borrowers.

Cash and cash equivalents as of December 31, 2012 were $5.484 billion, a decrease of $488 million or 8.2% from December 31, 2011. The decrease was primarily related to investment of cash associated with the QIL acquisition and a decrease in securities lending cash collateral offset by debt financing activity and a reduction of liquidity in the market.

Regarding fair value measurements, as of December 31, 2012, excluding separate accounts and other assets, the Company reflected $4.698 billion (7.0%) 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, 2012, the Company reported $60.570 billion (90.3%) as level 2, consisting primarily of various fixed maturity securities. Finally, the Company reported $1.811 billion (2.7%) 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, 2012, no single issuer, excluding U.S. Treasuries, agency securities and mortgage-backed securities, accounted for more than 1.6% of invested assets.

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

$ in Millions **December 31, 2012**	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
U.S. government and agency securities	$3,248	$281	($1)	$3,528
Residential MBS [1]	8,259	530	(4)	8,785
Commercial MBS	1,649	78	(1)	1,726
Other MBS and ABS [2]	2,332	155	(1)	2,486
U.S. state and municipal	13,235	1,350	(19)	14,566
Corporate and other	24,803	2,185	(53)	26,935
Foreign government securities	5,840	276	(48)	6,068
Total fixed maturities	59,366	4,855	(127)	64,094
Common stock	1,791	369	(63)	2,097
Preferred stock	422	25	(49)	398
Total equity securities	2,213	394	(112)	2,495
Total securities available for sale	$61,579	$5,249	($239)	$66,589

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

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

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

$ in Millions	As of December 31, 2012							
Mortgage & Asset-Backed Fixed Maturities by Credit Quality[1]	**AAA**	**AA**	**A**	**BBB**	**BB**	**B or Lower**	**Total**	**% of Total**
SBA loans	$2,085	$-	$-	$-	$-	$-	$2,085	16.0%
GNMA residential mortgage	3,262	5	-	-	-	-	3,267	25.1
FNMA residential mortgage	2,562	-	-	-	-	-	2,562	19.7
FHLMC residential mortgage	2,459	1	-	-	-	-	2,460	18.9
Prime residential mortgage	11	9	14	15	5	214	268	2.1
Alt-A residential mortgage	-	18	-	8	15	127	168	1.3
Sub-prime residential mortgage	27	-	3	1	6	23	60	0.5
Commercial MBS	1,623	68	7	26	2	-	1,726	13.3
Non-mortgage ABS	223	15	49	94	6	14	401	3.1
Total	$12,252	$116	$73	$144	$34	$378	$12,997	100.0%
% of Total	94.3%	0.9%	0.5%	1.1%	0.3%	2.9%	100.0%	

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

Approximately 80% of the Company's securitized portfolio is explicitly backed by the U.S. government (SBA and GNMA) or by government-sponsored entities (FNMA and FHLMC). Over 94% of the mortgage and asset-backed holdings are rated AAA. The commercial mortgage-backed securities portfolio is well diversified and of high quality with approximately 98% rated AA or above with approximately 13% 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, 2012 and December 31, 2011:

$ in Millions	As of December 31, 2012		As of December 31, 2011	
Fixed Maturities by Credit Quality[1]	**Fair Value**	**% of Total**	**Fair Value**	**% of Total**
AAA	$22,015	34.3%	$21,732	36.0%
AA+, AA, AA-	10,993	17.2	10,445	17.2
A+, A, A-	13,913	21.7	11,646	19.2
BBB+, BBB, BBB-	11,865	18.5	10,289	17.0
BB+, BB, BB-	1,523	2.4	2,202	3.6
B+, B, B-	2,889	4.5	3,330	5.5
CCC or lower	896	1.4	932	1.5
Total fixed maturities	$64,094	100.0%	$60,576	100.0%

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

The Company's allocation to investment grade (fixed maturities with an average credit rating of BBB- or higher) securities increased to 92% at December 31, 2012 from 89% at December 31, 2011. The increase in investment grade securities was related to a tactical portfolio realignment. Overall, the average credit quality rating stands at A+ as of December 31, 2012. The Company's holdings of below investment grade securities primarily consist of an actively managed diversified portfolio of high yield securities and loans within the domestic insurance portfolios and investments in emerging market sovereign and corporate debt primarily in support of the Company's international insurance operations.

The following table summarizes available-for-sale fixed maturity securities by contractual maturity at December 31, 2012 and December 31, 2011. Actual maturities may differ from contractual maturities because certain securities may be called or prepaid with or without call or prepayment penalties. Due to potential for prepayment on MBS and ABS, they are not categorized by contractual maturity.

$ in Millions	**As of December 31, 2012**		**As of December 31, 2011**	
Fixed Maturities by Maturity Date	**Fair Value**	**% of Total**	**Fair Value**	**% of Total**
1 year or less	$3,337	5.2%	$2,847	4.7%
Over 1 year through 5 years	19,275	30.1	17,738	29.3
Over 5 years through 10 years	15,808	24.7	14,489	23.9
Over 10 years	12,677	19.7	12,073	19.9
MBS and ABS	12,997	20.3	13,429	22.2
Total fixed maturities	$64,094	100.0%	$60,576	100.0%

During 2012, after taking into consideration changes in investment opportunities and its view of the current and prospective business and economic environment, the Company has 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, 2012 and 2011:

$ in Millions	**Three Months Ended December 31,**		**Twelve Months Ended December 31,**	
Net Investment Income	**2012**	**2011**	**2012**	**2011**
Taxable interest income	$596	$632	$2,467	$2,487
Tax-exempt interest income	111	124	449	474
Dividends	17	12	60	50
LP and LLC income	99	107	353	583
Commercial mortgage loans	21	19	81	77
Other investment loss	(13)	(1)	(22)	(4)
Gross investment income	831	893	3,388	3,667
Investment expenses	(43)	(40)	(151)	(144)
Net investment income	$788	$853	$3,237	$3,523

Net investment income for the three and twelve months ended December 31, 2012 was $788 million and $3.237 billion, respectively, decreases of $65 million and $286 million from the same periods in 2011. The decreases in the year and to a lesser extent in the quarter reflect lower valuation increases in LP and LLC investments. In addition, both periods reflect a decrease in taxable interest income due to lower investment yields primarily attributable to a tactical portfolio realignment.

Net Realized Gains (Losses)

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

$ in Millions Net Realized Gains (Losses)	Sales & Dispositions	Impairments	Change in Derivatives Value	Total
Three Months Ended December 31, 2012:				
Fixed maturities	$53	($1)	$-	$52
Common and preferred stock	(10)	(19)	-	(29)
Other	195	(13)	(20)	162
Total	$238	($33)	($20)	$185
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)

$ in Millions Net Realized Gains (Losses)	Sales & Dispositions	Impairments	Change in Derivatives Value	Total
Twelve Months Ended December 31, 2012:				
Fixed maturities	$291	($46)	$-	$245
Common and preferred stock	56	(56)	-	-
Other	337	(13)	(35)	289
Total	$684	($115)	($35)	$534
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

$ in Millions	Three Months Ended December 31,		Twelve Months Ended December 31,	
Components of Net Realized Gains (Losses)	**2012**	**2011**	**2012**	**2011**
Fixed maturities:				
Gross realized gains	$69	$37	$352	$177
Gross realized losses	(17)	(32)	(107)	(122)
Common and preferred stock:				
Gross realized gains	-	10	76	101
Gross realized losses	(29)	(39)	(76)	(73)
Other:				
Gross realized gains	203	20	367	105
Gross realized losses	(41)	(6)	(78)	(30)
Total net realized gains (losses)	$185	($10)	$534	$ 158

Net realized gains for the three and twelve months ended December 31, 2012 were $185 million and $534 million, respectively, increases of $195 million and $376 million over the same periods in 2011. The increases in the quarter and year primarily relate to gains recognized from security sales as part of a tactical portfolio realignment and gains on the sale of investments in the energy sector. Additionally, the year was impacted by a gain recognized from the sale of a business segment in Argentina and contingent consideration recognized in connection with the prior sale of certain Commercial Insurance policy renewal rights in 2009, partially offset by increased impairments due to market volatility.

The following table summarizes the Company's unrealized losses and fair value by security type and by duration as of December 31, 2012 that are not deemed to be other-than-temporarily impaired:

$ in Millions	**Less Than 12 Months**		**12 Months or Longer**	
Unrealized Losses & Fair Value by Security Type	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**
U.S. Government and agency securities	($1)	$405	$−	$−
Residential MBS	(1)	135	(3)	49
Commercial MBS	−	45	(1)	20
Other MBS and ABS	−	34	(1)	8
U.S. state and municipal	(9)	654	(10)	69
Corporate and other	(19)	1,250	(34)	417
Foreign government securities	(7)	439	(41)	438
Total fixed maturities	(37)	2,962	(90)	1,001
Common stock	(33)	354	(30)	215
Preferred stock	−	−	(49)	268
Total equity securities	(33)	354	(79)	483
Total securities available for sale	($70)	$3,316	($169)	$1,484

Unrealized losses decreased from $728 million as of December 31, 2011 to $239 million as of December 31, 2012 primarily due to the tightening of credit spreads and improvement in the equity markets. Unrealized losses less than 12 months decreased from $311 million at December 31, 2011 to $70 million as of December 31, 2012. Unrealized losses 12 months or longer decreased from $417 million as of December 31, 2011 to $169 million as of December 31, 2012. Of the $30 million unrealized losses 12 months or longer on common stock, $12 million relates to securities associated with non-guaranteed unit linked products where the policyholder bears the investment risk. As of December 31, 2012, there were 921 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 maturity 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 maturity securities, then the carrying value of the investment is written down to the expected cash flow amount and a realized loss is recorded as a credit impairment. A non-credit impairment loss is recognized in other comprehensive income, net of applicable taxes, as the difference between expected cash flows and fair value. For the three and twelve months ended December 31, 2012, the Company recorded $1 million and $46 million of fixed maturity impairment losses. The Company has concluded that the remaining gross unrealized losses of fixed maturity securities as of December 31, 2012 are temporary.

For equity securities, if the decline is believed to be other-than-temporary, the carrying value of the investment is written down to fair value and a realized loss is recorded. The gross unrealized losses recorded on equity securities at December 31, 2012 resulted primarily from decreases in quoted fair values from the dates that certain investment securities were acquired as opposed to fundamental changes in the issuer's financial performance and near-term financial prospects. For the three and twelve months ended December 31, 2012, the Company recorded $19 million and $56 million in impairment losses on equity securities. The Company has concluded that the gross unrealized losses of equity securities as of December 31, 2012 are temporary.

LIQUIDITY AND CAPITAL RESOURCES

General

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

Net cash flows are generally invested in marketable securities while keeping a certain amount in cash and short-term investments to meet unpredictable cash obligations. The Company monitors the duration of these investments, and purchases and sales are executed with the objective of having adequate cash available to satisfy its maturing liabilities. As the Company's investment strategy focuses on overall asset and liability durations, and not specific cash flows, asset sales may be required to satisfy obligations or rebalance asset portfolios. The Company's invested assets as of December 31, 2012 (including cash and cash equivalents) totaled $78.060 billion.

Debt outstanding as of December 31, 2012 and December 31, 2011 was as follows:

Current maturities of long-term debt:

$ in Millions	**As of December 31, 2012**	**As of December 31, 2011**
Current maturities of long-term debt[1]	$286	$205

[1] 2012 includes $25 million of 7.86% Medium Term Notes due 5/31/2013 and $260 million of 8.00% Notes due 10/31/2013. 2011 includes $204 million of debt originally issued by Safeco ($187 million was exchanged for like kind Liberty Mutual Group Inc ("LMGI"). debt in 2008) due 9/1/2012.

Long-term debt:

$ in Millions	As of December 31, 2012	As of December 31, 2011
7.86% Medium term notes, due 2013	$ -	$25
8.00% Notes, due 2013	-	260
5.75% Notes, due 2014	239	500
7.30% Notes, due 2014	104	200
5.588% Mortgage loan, due 2015	47	48
6.70% Notes, due 2016	249	249
7.00% Junior Subordinated notes, due 2067[1]	300	300
5.00% Notes, due 2021	600	600
4.95% Notes, due 2022	750	-
8.50% Surplus notes, due 2025	140	140
7.875% Surplus notes, due 2026	227	227
7.625% Notes, due 2028	3	3
3.91% - 4.25% Term loan, due 2032	300	-
7.00% Notes, due 2034	231	231
6.50% Notes, due 2035	471	471
7.50% Notes, due 2036	19	19
7.80% Junior Subordinated notes, due 2087[2]	700	700
10.75% Junior Subordinated notes, due 2088[3]	620	981
6.50% Notes, due 2042	750	-
7.697% Surplus notes, due 2097	260	435
Subtotal	6,010	5,389
Unamortized discount	(20)	(48)
Total long-term	$5,990	$5,341

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

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

Debt Transactions and In-force Credit Facilities

On December 20, 2012, Liberty Mutual Insurance Company ("LMIC") entered into a three-year $1 billion repurchase agreement which terminates on December 20, 2015. To date, no funds have been borrowed under the facility. In connection with the new facility, the Company terminated its $1 billion three-year repurchase agreements dated March 26, 2010.

On May 4, 2012 and August 17, 2012, LMGI issued $500 million and $250 million of Senior Notes due 2022 (the "2022 Notes"), respectively. Also, on May 4, 2012 and August 17, 2012, LMGI issued $500 million and $250 million of Senior Notes due 2042 (the "2042 Notes"), respectively. Interest is payable semi-annually at a fixed rate of 4.95% for the 2022 Notes and 6.50% for the 2042 Notes. The 2022 Notes mature on May 1, 2022 and the 2042 Notes mature on May 1, 2042.

On April 18, 2012, the Company announced the commencement of two tender offers. The first offer was a cash tender offer to purchase up to $350 million, subject to increase, of the aggregate principal amount of (i) LMGI's 10.75% Series C Junior Subordinated Notes due 2088 by LMGI and (ii) LMIC's 7.697% Surplus Notes due 2097 by LMIC, each at a purchase price determined in accordance with the procedures of a modified "Dutch Auction" (the "Dutch Auction Offer"). The second offer was a cash tender offer by LMGI to purchase up to $350 million, subject to increase, of the aggregate principal amount of its 5.75%

Senior Notes due 2014 and its 7.30% Senior Notes due 2014, each at a price determined by reference to a fixed spread above the bid-side yield on the applicable reference security and accepted in accordance with the acceptance priority level set forth in the tender documents (the "Waterfall Offer"). The Waterfall Offer was conditioned on LMGI issuing at least $350 million aggregate principal amount of new senior notes. The Waterfall Offer was increased to include all notes tendered in the Waterfall Offer. The Dutch Auction Offer was increased by up to $175 million in aggregate principal amount to permit the additional purchase of the applicable notes tendered at the full tender offer consideration. The tender offers expired on May 15, 2012 and the Company paid in aggregate approximately $949 million in connection with such tender offers, including approximately $17 million in accrued and unpaid interest, to holders of the Notes involved in the tender offers. As a result of these transactions, the Company recorded pre-tax losses of $147 million that are included in loss on extinguishment of debt in the accompanying consolidated statements of income. After completion of the tender offers, the following principal amounts remained outstanding for such notes, $676 million of the 10.75% Series C Junior Subordinated Notes due 2088, $260 million of the 7.697% Surplus Notes due 2097, $239 million of the 5.75% Senior Notes due 2014 and $104 million of the 7.30% Senior Notes due 2014.

Additionally, during the three and twelve months ended December 31, 2012, the Company repurchased $56 million and $97 million, respectively, of the 10.75% Junior Subordinated Notes due 2088. Pre-tax losses of $30 million and $46 million, respectively, were recorded on these transactions and are included in loss on extinguishment of debt in the accompanying consolidated statements of income. During the three and twelve months ended December 31, 2011, the Company repurchased $135 million and $269 million, respectively, of the 10.75% Junior Subordinated notes due 2088. 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 statements of income.

LMIC, Peerless Insurance Company ("PIC"), Liberty Life Assurance Company of Boston ("LLAC"), Liberty Mutual Fire Insurance Company ("LMFIC") and Employers Insurance Company of Wausau ("EICOW") are members of the Federal Home Loan Bank. On March 21, 2012, LMFIC borrowed $150 million at a rate of 3.91% with a maturity date of March 22, 2032. On March 23, 2012 and April 2, 2012, LMIC borrowed $127 million at a rate of 4.24% with a maturity date of March 23, 2032 and $23 million at a rate of 4.25% with a maturity date of April 2, 2032, respectively. As of December 31, 2012, all of the outstanding Federal Home Loan Bank borrowings are fully collateralized.

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

On October 24, 2011, LMAC and Ohio Casualty Corporation terminated their $200 million unsecured three-year 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, 2012, 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 in 2011. After completion of the tender offer and subsequent open market purchase, $19 million aggregate principal amount of the 2036 Notes remains outstanding.

Interest Expense

Consolidated interest expense for the three and twelve months ended December 31, 2012 was $105 million and $419 million, decreases of $1 million and $20 million from the same periods in 2011. The decrease reflects the completion of the tender offers, 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 new debt issuances. 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, 2012, the Company, through its downstream subsidiary LMGI, had $5.297 billion of debt outstanding, excluding discount.

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 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, 2012) and 2013 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	**2012**	**2011**	**2013**	**2012**
LMIC	457%	469%	$1,452	$65
LMFIC	343%	458%	-	$15
EICOW	567%	623%	-	-

[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, 2012. Available dividend capacity as of December 31, 2012 is calculated as 2013 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 advisor is entitled to recover annual expenses for investment management services performed by its employees.
- Liberty Corporate Services LLC (“LCS”), which through its subsidiaries collects fees and other revenues, primarily for claims administration and agency services rendered for affiliated and non-affiliated entities. For the three and twelve months ended December 31, 2012, LCS recorded $86 million and $406 million in pre-tax income.
- Approximately $80 million of annual dividends related to non-redeemable perpetual preferred stock issuances by LMIC and LMFIC.

Statutory Surplus

Statutory surplus as regards policyholders for the combined operations of LMIC and its U.S affiliates, including international branches, was $16.521 billion and $15.701 billion at December 31, 2012 and December 31, 2011, respectively. The increase in surplus reflects affiliated unrealized gains of $375 million, unaffiliated unrealized gains of $326 million, and other changes in surplus of $448 million, partially offset by repurchases of surplus notes ($172) million and a net loss of $157 million (the sum of earnings from the Company’s 58 domestic property-casualty insurance companies and dividends from subsidiaries). Other changes in surplus are driven by increases in capital contributions and net deferred tax assets, partially offset by increases in dividends to stockholders and non-admitted assets.

CRITICAL ACCOUNTING POLICIES

Critical Accounting Estimates

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

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

Certain reclassifications have been made to the 2010 and 2011 amounts to conform with the 2012 presentation.

Adoption of New Accounting Standards

In October 2010, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2010-26, *Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts* ("ASU 2010-26"). This guidance, as codified in 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 was required to adopt ASU 2010-26 effective January 1, 2012. The Company applied the guidance retrospectively, and the cumulative effect of the adoption as of January 1, 2010 resulted in (decreases) increases in the opening balance of unassigned equity and accumulated other comprehensive income of $(286) million and $2 million, respectively. The impact to the consolidated statements of income for the year ended December 31, 2012 is immaterial.

For the year ended December 31, 2011, the accounting change resulted in (decreases) increases in benefits, claims and claim adjustment expenses, insurance operating costs and expenses, amortization of deferred policy acquisition costs, income tax (benefit) expense, unrealized gains on securities, and foreign currency translation and other adjustments of $(3) million, $692 million, $(678) million, $(4) million, $4 million, and $1 million, respectively. For the year ended December 31, 2010, the accounting change resulted in (decreases) increases in benefits, claims and claim adjustment expenses, insurance operating costs and expenses, amortization of deferred policy acquisition costs, income tax (benefit) expense, unrealized gains on securities, and foreign currency translation and other adjustments of $(4) million, $699 million, $(722) million, $10 million, $2 million, and $2 million, respectively. As of December 31, 2011, the accounting change resulted in the following changes to previously reported balances: (decreases) increases in deferred acquisition costs, deferred income taxes, life unpaid claims and claim adjustment expenses and future policy benefits, other liabilities, unassigned equity, and accumulated other comprehensive income of $(417) million, $137 million, $(12) million, $(3) million, $(276) million, and $11 million, respectively.

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

Future Adoption of New Accounting Standards
None of the accounting standards issued in 2012 will have a material impact on the Company in the future.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were $51.885 billion and $50.228 billion as of December 31, 2012 and December 31, 2011, respectively.

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

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

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

Asbestos and Environmental

The Company's asbestos and environmental reserves for unpaid claims and claim adjustment expenses, net of reinsurance decreased $117 million from $1.332 billion as of December 31, 2011 to $1.215 billion as of December 31, 2012.

In the third quarter of 2011, the Company completed asbestos ground-up and aggregate environmental reserve studies. These studies were completed by a multi-disciplinary team of internal claims, legal, reinsurance and actuarial personnel, and included all major business segments of the Company's direct, assumed, and ceded asbestos and environmental unpaid claim liabilities. As part of the internal review, policyholders with the largest direct asbestos unpaid claim liabilities were individually evaluated using the Company's proprietary stochastic ground-up model, which is consistent with published actuarial methods of 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, injury type, jurisdiction and legal defenses. Reinsurance recoveries for these policyholders were then separately evaluated by the Company's reinsurance and actuarial personnel. Asbestos and environmental unpaid claim liabilities for all other policyholders were evaluated using aggregate methods that utilized information and experience specific to these policyholders. 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 a 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 $13.232 billion and $13.272 billion at December 31, 2012 and December 31, 2011, respectively, net of allowance for doubtful accounts of $275 million and $326 million, respectively. Included in these balances are $905 million and $941 million of paid recoverables and $12.602 billion and $12.657 billion of unpaid recoverables, respectively.

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

As part of its reinsurance security oversight, the Company has established a Reinsurance Credit Committee (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 96% and 94% 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, 2012. Collateral held against outstanding gross reinsurance recoverable balances was $4.838 billion and $4.699 billion at December 31, 2012 and December 31, 2011, respectively.

The remaining 4% and 6% 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, 2012.

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

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, 2012 and 2011, deferred gains related to these reinsurance arrangements were $296 million and $315 million, respectively, and are included in other liabilities within the accompanying consolidated balance sheets. Interest credited to the funds held balances for the years ended December 31, 2012, 2011, and 2010 was $83 million, $105 million, and $118 million, respectively. Deferred gain amortization was $29 million, $129 million, and $54 million for the years ended December 31, 2012, 2011, and 2010, respectively. Reinsurance recoverables related to these transactions, including experience related profit accruals, were $1.165 billion and $1.217 billion as of December 31, 2012 and 2011, respectively. Effective March 31, 2011, the Company commuted two workers compensation excess of loss retroactive reinsurance agreements. The commutations, which represent the complete and final settlement and discharge of all present and future obligations between the parties arising out of the agreements, resulted in a gain to the Company of $54 million, net of tax.

Additionally, the Company has an aggregate stop loss program covering substantially all of Legacy 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. Additional premium and loss activity on these retroactive and prospective contracts was immaterial in 2012 and 2010. 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. The impact to the accompanying consolidated statements of income from 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.

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

Impairment Losses on Investments

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

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

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

Variable Interest Entities

The Company invests in energy, private equity and real estate limited partnerships and other entities subject to variable interest entity ("VIE") analysis under the VIE subsections of ASC 810, *Consolidation*. The Company analyzes each investment to determine whether it is a VIE, and if so, whether the Company is the primary beneficiary or a significant interest holder based on a qualitative and quantitative assessment. The Company evaluates the design of the entity, the risks to which the entity was designed to expose the variable interest holder and the extent of the Company's control of and variable interest in the VIE. As of December 31, 2012 the Company has determined that it is the primary beneficiary of one VIE in the low-income housing tax credit sector, and as such, this VIE has been consolidated in the Company's financial statements. As of December 31, 2011, the Company determined that it was the primary beneficiary of one VIE in the energy investment sector, and as such, this VIE was consolidated in the Company's financial statements. As of December 31, 2012, this entity is no longer deemed a VIE and therefore no longer consolidated. The carrying value of assets and liabilities, and the Company's maximum exposure to loss of the consolidated VIE's as of December 31. 2012 and 2011 was 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*. These VIEs are principally private equity limited partnerships in which the Company has invested as a passive limited partner. The partnerships were deemed to be VIEs because the equity holders as a group lack the power to direct the activities that most significantly impact the respective entity's economic performance. The VIEs generate variability primarily from investment portfolio performance and that variability is passed to equity holders. For these VIEs, the Company absorbs a portion, but not a majority, of this variability. The net carrying value of non consolidated VIEs in which the Company has a significant variable interest was $282 million and $250 million as of December 31, 2012 and December 31, 2011, respectively, and the Company's maximum exposure to loss was $340 million and $309 million as of December 31, 2012 and December 31, 2011, respectively. The assets are included in Other Investments on the accompanying consolidated balance sheets. Maximum exposure to loss includes the carrying value and unfunded commitment of the VIEs. There is no recourse provision to the general credit of the Company for any VIEs beyond the full amount of the Company's loss exposure.

Deferred Acquisition Costs

Total deferred acquisition costs were $2.732 billion and $2.391 billion as of December 31, 2012 and December 31, 2011, respectively. Deferred acquisition costs are costs that are directly related to the acquisition or renewal of insurance contracts. All other acquisition related costs, including market research, training, administration, unsuccessful acquisition or renewal efforts, and product development, are charged to expense as incurred. Deferred acquisition costs are reviewed annually for recoverability. Investment income is considered in the recoverability assessment. For short-duration insurance contracts, acquisition costs include commissions, underwriting expenses, and premium taxes and assessments. For long-duration insurance contracts, these costs include first year commissions in excess of annual renewal commissions and variable sales and underwriting expenses.

Goodwill

Goodwill assets were $4.850 billion and $4.766 billion as of December 31, 2012 and December 31, 2011, respectively. Goodwill is tested for impairment at least annually using either a qualitative or a quantitative process. Election of the approach can be made at the reporting unit level. The reporting unit has the option to skip the qualitative test and move directly to completion of the quantitative process. The Company's SBUs are deemed reporting units. The 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.

As a result of the realignment of the Company's SBUs on July 24, 2012, the Company performed a relative fair value assessment to reallocate the existing goodwill to the SBUs. In conjunction with the reallocation the Company performed a quantitative impairment assessment of goodwill for each of the SBUs. In line with the Company's annual impairment testing timeline, a qualitative test was performed by each SBU as of August 31, 2012. In 2011, the Company utilized the qualitative and quantitative approaches across its business units.

Deferred Income Taxes

The net deferred tax asset was $1.102 billion and $952 million as of December 31, 2012 and December 31, 2011, net of a valuation allowance of $185 million and $136 million respectively. The net increase in the Company's net deferred income tax asset is primarily due to net operating losses, offset by an increase in the deferred tax liability for net unrealized capital gains on investments. The increase in the valuation allowance is primarily due to net operating losses generated in certain foreign subsidiaries where there is uncertainty in the timing and amount of realization of those losses. Management believes it is more likely than not that the Company's net deferred income tax asset will be realized based upon the Company's ability and the likelihood of generating future taxable income.

The income tax provision is calculated under the liability method. Deferred income tax assets and liabilities are recorded based upon the difference between the financial statement and tax bases of assets and liabilities at the enacted tax rates. The principal assets and liabilities giving rise to such differences are net unrealized capital gains and losses on 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:

Balance at December 31, 2011	$332
Additions based on tax positions related to current year	23
Reductions based on tax positions related to current year	(31)
Additions for tax positions of prior years	81
Reductions for tax positions of prior years	(47)
Settlements	(2)
Balance at December 31, 2012	$356

Included in the tabular roll forward of unrecognized tax benefits are interest and penalties in the amount of $102 million and $78 million as of December 31, 2012 and December 31, 2011, respectively.

Included in the balance at December 31, 2012, is $188 million related to tax positions that would impact the effective tax rate.

The Company recognizes interest and penalties in Federal, state, and foreign income tax expense. During the three months ended December 31, 2012 and 2011, the Company recognized approximately $8 million and $(2) million in interest and penalties, respectively. During the years ended December 31, 2012 and 2011, the Company recognized $15 million and $2 million in interest and penalties, respectively. The Company had approximately $106 million and $82 million of interest and penalties accrued at December 31, 2012 and December 31, 2011, respectively.

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

The IRS has completed its review of the Company's federal income tax returns through the 2001 tax year and is currently reviewing income tax returns for the 2002 through 2009 tax years. Any adjustments that may result from the IRS examinations of these income tax returns are not expected to have a material impact on the financial position, liquidity, or results of operations of the Company.

About the Company

Boston-based LMHC, the parent corporation of the Liberty Mutual Insurance group of entities, is a diversified global insurer and third largest property and casualty insurer in the U.S. based on 2011 direct written premium. The Company also ranks 84th on the Fortune 100 list of largest corporations in the U.S. based on 2011 revenue. As of December 31, 2012, LMHC had $120.060 billion in consolidated assets, $101.535 billion in consolidated liabilities, and $36.944 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 strategic business units, with each operating independently of the others with 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 50,000 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.